

Stephen David Prowse, Ph.D.

March 5, 2010

New York, NY

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1 UNITED STATES DISTRICT COURT

2 FOR THE SOUTHERN DISTRICT OF NEW YORK

3 -----

4 SECURITIES AND EXCHANGE COMMISSION,

5 Plaintiff,

6 v.

7 ANDREAS BADIAN, et al.,

8 Defendants.

9

10 CIVIL ACTION NO. 06-CV-2621 LTS (DFE)

11 -----

12 VIDEOTAPED DEPOSITION OF

13 STEPHEN DAVID PROWSE, Ph.D.

14 March 5, 2010

15

16 T R A N S C R I P T of the deposition

17 taken before BRIDGET LOMBARDOZZI, a Certified

18 Shorthand Reporter, CRR, RMR, RPR, and Notary

19 Public of the State of New York, at the

20 offices the SECURITIES AND EXCHANGE COMMISSION,

21 3 World Financial Center, New York, New York,

22 on March 5, 2010, commencing at 10:07 a.m.

23

24 Reported by:

25 Bridget Lombardozzi, CSR, RMR, CRR, CLR

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<p>1 APPEARANCES:</p> <p>2 SECURITIES AND EXCHANGE COMMISSION</p> <p>3 Attorneys for the Plaintiff</p> <p>4 100 F Street N.E.</p> <p>5 Washington, D.C. 20549</p> <p>6 202.551.4480</p> <p>7 BY: KENNETH J. GUIDO, ESQUIRE</p> <p>8</p> <p>9 DLA PIPER LLP (US)</p> <p>10 Attorneys for Defendant Andreas Badian</p> <p>11 and the Witness</p> <p>12 1251 Avenue of the Americas</p> <p>13 New York, New York 10020-1104</p> <p>14 212.335.4892</p> <p>15 BY: JOSHUA S. SOHN, ESQUIRE</p> <p>16 CARYN G. SCHECHTMAN, ESQUIRE</p> <p>17 MEGAN VESELY, ESQUIRE</p> <p>18</p> <p>19 ALSO PRESENT:</p> <p>20 FREDERICK C. DUNBAR, US SEC</p> <p>21 LAWRENCE R. GLOSTEN</p> <p>22 CHARLES M. JONES</p> <p>23 JONATHAN CLAY, Videographer</p> <p>24</p> <p>25</p>	<p>1 PREVIOUSLY MARKED EXHIBITS (continued):</p> <p>2 EXHIBIT 86 Page 210</p> <p>3 EXHIBIT 87 Page 210</p> <p>4 EXHIBIT 88 Page 210</p> <p>5 EXHIBIT 89 Page 210</p> <p>6 EXHIBIT 90 Page 210</p> <p>7 EXHIBIT 10 Page 220</p> <p>8 EXHIBIT 57 Page 241</p> <p>9 EXHIBIT 47 Page 242</p> <p>10</p> <p>11</p> <p>12</p> <p>13</p> <p>14</p> <p>15</p> <p>16</p> <p>17</p> <p>18</p> <p>19</p> <p>20</p> <p>21</p> <p>22</p> <p>23</p> <p>24</p> <p>25</p>
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<p>1 - STEPHEN D. PROWSE - 2 THE VIDEOGRAPHER: Will the court 3 reporter please administer the oath. 4 STEPHEN D AVID 5 PROWSE, Ph.D., FTI Consulting, 2001 Ross 6 Avenue, Suite 400, Dallas, Texas, having been 7 duly sworn, testified as follows: 8 DIRECT-EXAMINATION 9 BY MR. GUIDO: 10 Q. Will you state your full name for 11 the record, please? 12 A. Stephen David Prowse. 13 Q. Where are you employed? 14 A. I'm employed at a company called 15 FTI Consulting. 16 Q. How long have you been there? 17 A. I've been at FTI Consulting since 18 November of 2003. 19 Q. Were you retained to be an expert 20 in this litigation? 21 A. Yes. 22 MR. GUIDO: I'd like to have the 23 court reporter hand you what I've marked as 24 Exhibit No. 21. It's a premarked exhibit. The 25 court reporter has it.</p>	<p>1 - STEPHEN D. PROWSE - 2 you wish to use to refer to it. But I will be 3 referring to Badian's trading. 4 So if you want to each time 5 clarify that in your view it's Rhino trading, 6 I'm perfectly happy for you to do so. 7 But my question was: Were you 8 retained to do an -- a study of Badian's 9 trading of Sedona stock? 10 A. I was retained in this matter to 11 do a study of Rhino's trading of Sedona stock, 12 yes, understanding that clarification. 13 Q. Now -- and prior to that time, you 14 had not examined the trading in Sedona stock? 15 A. Prior to that time, I had not done 16 any examination of trading in Sedona stock. 17 Q. And what did you do after you were 18 retained on November 4th, 2009, to prepare for 19 the expert report that you provided in this 20 case? 21 A. Well, Mr. Beloreshki and I were 22 hired as joint experts in this matter. So 23 after I was retained, I discussed with him the 24 matter and the appropriate approach to answer 25 the questions that we were asked to address.</p>
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<p>1 - STEPHEN D. PROWSE - 2 THE REPORTER: I gave it back to 3 you, sir. 4 MR. GUIDO: She did, and I don't 5 have it. 6 MR. SOHN: Mark this one. 7 (Whereupon, exhibit is received and 8 marked BP-21 for identification.) 9 BY MR. GUIDO: 10 Q. Is Exhibit 21 the letter of 11 retention that you signed on November 4th, 12 2009, to appear as an expert witness in this 13 matter? 14 MR. SOHN: Objection to form. 15 A. Yes, this is the one I signed. 16 Q. Now, prior to November 4th, 2009, 17 had you done any work with regard to the 18 Sedona's trading -- I mean the trading by 19 Andreas Badian in the Sedona stock? 20 A. I have not done any work with 21 regards to Rhino trading in Sedona stock prior 22 to being retained on this matter. 23 Q. For definitional purposes for the 24 record, I'll be referring to Badian's trading 25 and you're perfectly free to use whatever term</p>	<p>1 - STEPHEN D. PROWSE - 2 And based on our -- our discussion 3 with -- based on my discussion with him, we 4 proceeded to perform the analysis. 5 Q. Okay. Will you take a look at -- 6 in front of you in the blue batch are the 7 exhibits from Mr. Beloreshki's deposition. 8 I'll be using them in this deposition. 9 And I'd like you to take a look at 10 Exhibit No. 4. 11 MR. JONES: I think it's not on 12 top. 13 MR. SOHN: Number 1's on top. 14 MR. JONES: You're good. 15 (Whereupon, there is a pause in 16 the proceedings.) 17 BY MR. GUIDO: 18 Q. Have you had a chance to review 19 Exhibit No. 4? 20 A. Yes. 21 Q. Okay. Is that the expert report 22 that you prepared in this matter? 23 A. Yes, it is. 24 Q. Okay. Now, what documents did you 25 review prior to signing this report? I think</p>

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<p>1 - STEPHEN D. PROWSE - 2 the date is November 24th? 3 A. November 24th, correct. 4 Q. What documents did you review? 5 A. The documents I reviewed, I 6 believe, would be listed in Exhibit 3. These 7 would be documents I directly reviewed, or the 8 team that was working on the engagement 9 reviewed. 10 Q. Pardon? 11 A. The team that was working on the 12 engagement reviewed. 13 Q. I asked what you reviewed. 14 A. I reviewed -- I reviewed the 15 Complaint; I reviewed the responses and 16 objections, and the first supplemental 17 responses and objections; I reviewed the audit 18 trail reports. I believe I reviewed some of 19 these individual numbered Bates documents, if 20 not all of them. I reviewed the trading data 21 which was in electronic format. And I may 22 have reviewed some of these account statements. 23 I reviewed the Chaplinsky and Haushalter 24 article. 25 Q. Pardon?</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. Can you tell us what literature 3 that is? 4 A. There's a Hillion and Vermaelen 5 article that would have appeared, I believe, in 6 the Journal of Financial Economics. There is 7 Mr. Beloreshki's article. There is -- 8 Q. What article is that? 9 MR. SOHN: Mr. Guido, can you 10 please let the witness finish? 11 MR. GUIDO: I'm sorry. 12 A. That is the article that you 13 questioned him about on Tuesday, I believe. 14 Q. The one that you co-authored 15 with -- 16 A. Yes. 17 Q. -- Mr. Beloreshki? 18 A. Yes. 19 There may be -- there may be other 20 articles that are on the broad topic of PIPEs 21 or future price securities out there that I 22 have read before, but I can't -- they don't 23 come to mind as I sit here. 24 Q. Well, when you were sitting there 25 and you were preparing the report, did they</p>
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<p>1 - STEPHEN D. PROWSE - 2 A. I reviewed the Chaplinsky and 3 Haushalter article. And I reviewed various 4 data from Bloomberg, from FactSet, from the 5 NBER, and reviewed various SEC filings. 6 Q. Well, let me ask you something: 7 How did you obtain the Chaplinsky article to 8 review? 9 A. I can't remember. I may have had 10 it. I may individually have had it, a hard 11 copy of it. 12 Q. What is your understanding of the 13 subject matter of that paper? 14 A. That it looks at -- it examines 15 the financial characteristics of certain -- of 16 PIPEs, private investments in public equity, 17 and looks at the characteristics of firms that 18 are issuing them and performs some -- a variety 19 of economic tests. And -- 20 Q. Did you review any other 21 literature that covered that subject matter? 22 A. For this particular engagement, 23 no. I'm aware of other literature out there 24 that talks about the -- similar to the 25 Chaplinsky and Haushalter article.</p>	<p>1 - STEPHEN D. PROWSE - 2 come to mind? 3 A. I didn't review them specifically 4 for the report, but my body of knowledge that 5 is -- that has been accumulated over 25 years 6 doing economics, or longer, it's -- it's just 7 sitting there as general awareness and general 8 knowledge of what the literature says and 9 what -- what some people have written. 10 Q. Okay. Let's take Mr. Beloreshki's 11 article. Okay? 12 A. Uh-huh. 13 Q. In his article, does he address 14 the question of the motivation of people that 15 bring lawsuits contending that the prices of 16 stock have been manipulated? 17 A. Does he address the motivation of 18 people bringing lawsuits? 19 Q. Alleging market manipulation. 20 A. He may talk about that. 21 Q. Well, what did he say? 22 A. I can't recall specifically what 23 he said. 24 Q. What about -- 25 A. I'd be happy to look at the</p>

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<p>1 - STEPHEN D. PROWSE - 2 article if you want me to. 3 Q. We'll have to look at the 4 article? 5 A. I'd be happy to if you want me to 6 look at it. 7 Q. No, I understand that. You'd be 8 happy to look at the article. 9 A. Yeah. 10 Q. And what about Hildebrand? What 11 did they say about the motivations of people 12 who allege market manipulation? 13 A. Hildebrand? 14 Q. I think it was -- 15 A. I'm not aware of the person you 16 said, Hildebrand. 17 Q. I'm sorry. You mentioned -- I 18 thought that you said Hildebrand. 19 What was the -- what was the other 20 article that you said that you were aware of? 21 A. There were two authors: One 22 was -- one's surname is Hillion. 23 Q. Hillion, excuse me. 24 A. H-i-l-l-i-o-n. And the other's 25 surname Vermaelen, V-e-r-m-a-e-l-e-n, I think.</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. Do you know? 3 A. I haven't done a study of what FTI 4 has issued in terms of financing their 5 activities. I know they're buying back stock 6 just from my general knowledge, so... 7 It would be extremely surprising 8 to me if they had issued an FPS, as I 9 understand what an FPS is. But I wouldn't be 10 surprised maybe if they issued a convertible 11 bond. 12 Q. What do you understand an FPS 13 is? 14 A. A future -- well, FPSs can be 15 customized -- they're customized securities 16 between, you know, sophisticated entities. So 17 their terms can vary a lot. But, generally, I 18 would describe a future price security as a 19 convertible note that is convertible after some 20 lock-up period into the equity of the firm 21 issuing the bond or issuing the note at some 22 discount to a -- to a benchmark price that's 23 calculated based on some -- some measure of the 24 current stock price of the firm. 25 Q. Now, when you reviewed the -- or</p>
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<p>1 - STEPHEN D. PROWSE - 2 They're telling me I got that right. 3 Q. What was the subject matter of 4 that paper? 5 A. I don't believe they talked about 6 the motivations of bringing -- I don't believe 7 they talked about the motivations for people to 8 bring lawsuits alleging market manipulation in 9 that paper. I think it was more of a 10 descriptive analysis of the types of firms that 11 issue future price securities and how most of 12 them are extremely small, risky firms. 13 Q. Did F -- did FTI recently issue 14 future price securities? 15 A. I would be very surprised. Well, 16 what do you mean by that? Could you define a 17 future price security for me? 18 Q. Did it recently issue a 19 convertible debenture? 20 A. Well, that's a different -- that's 21 a different instrument than a future price 22 security. 23 Q. Okay. 24 A. So, they may have -- they may have 25 issued a convertible bond. I don't know.</p>	<p>1 - STEPHEN D. PROWSE - 2 when you were preparing your report, did you 3 review any literature on market 4 microstructure? 5 A. No, not for preparing this report. 6 I -- based on my training and my education, 7 I've obviously read a lot of articles on market 8 microstructure and that forms sort of the 9 background or base of my knowledge, but I did 10 not specifically review any for this -- for 11 this engagement. 12 Q. Did you review any literature that 13 related trading activity to price changes? 14 MR. SOHN: Anything? 15 MR. GUIDO: Any literature. 16 A. For this engagement? 17 Q. For this engagement. 18 A. No, I don't believe I did. 19 Q. Do you consider yourself an expert 20 on trading activity and price changes? 21 A. I would consider myself an expert 22 in financial economics, financial instruments 23 and financial markets, and understanding how to 24 measure the stock pricing impact of a news 25 announcement or an event or trade. I consider</p>

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<p>1 - STEPHEN D. PROWSE - 2 myself an expert in those areas. 3 Q. So, prior to this case and Pet 4 Quarters, had you ever done an analysis of the 5 relationship between trading activity and price 6 change? 7 A. Not in terms of my consulting 8 work, no. 9 Q. Okay. In any other context? 10 A. It may -- I may well have. I 11 believe I did do study courses on that for my 12 Ph.D. training. I reviewed articles and 13 studied articles on that as part of my Ph.D. 14 training in finance and economics. 15 Q. When did you get your Ph.D.? 16 A. I'm sorry? 17 Q. When did you get your Ph.D.? 18 A. 1989. 19 Q. 1989. So that's 20 years ago. 20 A. Yes. I may also have reviewed 21 literature around that topic for my CFA 22 charter. 23 Q. When did you get your CFA charter? 24 A. Nine -- 2001, I believe. 25 Q. Okay. So that was about nine</p>	<p>1 - STEPHEN D. PROWSE - 2 through impact -- trading impact on the stock. 3 There's various theories that have 4 been tested by and run by people such as 5 Professors Glosten and Jones. 6 Q. What did -- what sort of work did 7 Professor Glosten and Jones do that you just 8 referred to? 9 A. Various studies they've done. 10 Q. Well, can you name one of them? 11 A. I can -- I can't name the title of 12 it. It looks at the impact on price of 13 trading. 14 Q. And what -- it looks at the impact 15 of price on trading or trading on price? 16 A. On price of trading. 17 Q. On the price of trading. 18 And what does -- what does it 19 measure in terms of the impact on the price of 20 trading? 21 A. Well, I'd have to look at the 22 article to be -- to be able to tell you. I 23 can't sit here and -- 24 Q. Did you look at the article before 25 you --</p>
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<p>1 - STEPHEN D. PROWSE - 2 years ago. 3 A. Yes. 4 Q. Did you go back after you were 5 retained to prepare this report to review the 6 literature that you had studied in your Ph.D. 7 program and when you got your CFA on trading 8 activity and price changes? 9 A. I didn't -- I didn't review any 10 specific literature. I used my knowledge 11 gained as an economist for 25 years in 12 financial economics. 13 Q. The -- well, based on your 14 recollection of what you studied 10 and 20 15 years ago, can you tell us what theories of 16 price change in tradings are in the 17 literature? 18 MR. SOHN: Which literature? The 19 literature that he read 20 years ago? 20 Q. The ones you reviewed 20 years ago 21 and 10 years ago. 22 A. Yeah, I mean, there's various 23 theories about trading behavior and how it 24 affects the price through inventory 25 adjustments, through asymmetric information,</p>	<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: Mr. Guido, you -- 3 MR. GUIDO: Excuse me. 4 MR. SOHN: He wasn't finished with 5 his answer. 6 A. I'd have to look at the article 7 specifically to tell you exactly what they did 8 and exactly how they measured things. 9 Q. Well, did you look at their 10 articles before you wrote that report? 11 A. No. 12 Q. What does the -- what do the 13 articles that Professor Jones and Professor 14 Glosten wrote suggest about the appropriate 15 measure of active in determining prices? 16 A. Again, I'd have to look at the 17 specific article to be able to tell you. 18 Q. Okay. 19 A. I believe one of the things 20 they -- they look at is whether there's a trade 21 or not. 22 Q. Okay. Well, is one of the -- have 23 you seen any literature that indicates that -- 24 with regard to analyzing trading that buys move 25 prices up and sells move prices down?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I'm generally aware that I think</p> <p>3 there are some results that suggest that, yes.</p> <p>4 Q. Okay. And that -- how are buys</p> <p>5 defined in that literature?</p> <p>6 A. I think the literature would</p> <p>7 probably have different definitions of buys,</p> <p>8 depending on who's doing the study. I mean,</p> <p>9 there's lots of studies out there.</p> <p>10 Q. Well, is one of the definitions of</p> <p>11 buys are trades executed at the offer or above</p> <p>12 the offer?</p> <p>13 A. I don't know about -- above maybe.</p> <p>14 Yeah, could be.</p> <p>15 Q. Okay. And that sells are sells if</p> <p>16 the bidder put in a lower bid?</p> <p>17 A. That may be, too.</p> <p>18 Q. In fact, didn't -- didn't you have</p> <p>19 a -- such a study done in Pet Quarters?</p> <p>20 MR. SOHN: Objection.</p> <p>21 A. I'd have to see the Pet Quarters</p> <p>22 report to see exactly what you're referring to.</p> <p>23 We did an initial report and a rebuttal report.</p> <p>24 We did a lot of analysis in there. So I'd like</p> <p>25 to see the report to see exactly what you're</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, let me ask you, what is</p> <p>3 your understanding of why transactions move</p> <p>4 prices?</p> <p>5 A. Transactions can move prices for</p> <p>6 information reasons; for supply and demand</p> <p>7 reasons on the inventory of a broker. Reasons</p> <p>8 like that.</p> <p>9 Q. Well, in the papers that you</p> <p>10 studied 20 years ago and 10 years ago, did they</p> <p>11 suggest what the key measures of trading</p> <p>12 activity would be when looking to -- at price</p> <p>13 changes?</p> <p>14 A. I believe they used a variety of</p> <p>15 different trading measures, one of which is</p> <p>16 whether a trade occurred or not.</p> <p>17 Q. Well, can you tell us what</p> <p>18 literature says that?</p> <p>19 A. I think that's in the Glosten and</p> <p>20 Jones papers and other papers.</p> <p>21 Q. What are the other papers?</p> <p>22 A. Well, I can't name them</p> <p>23 specifically for you, but I know there's a body</p> <p>24 of literature out there.</p> <p>25 Q. Does the body of literature</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 referring to.</p> <p>3 Q. Well, in -- in the report --</p> <p>4 A. There were two reports.</p> <p>5 Q. There were two reports.</p> <p>6 A. Yes.</p> <p>7 Q. There was an initial report and</p> <p>8 there was -- there was a rebuttal report.</p> <p>9 A. Yes.</p> <p>10 Q. And was one of the reports -- one</p> <p>11 of the studies that you did, was the impact on</p> <p>12 purchases at the offer on the price of Pet</p> <p>13 Quarters stock?</p> <p>14 A. Sitting here, I'd have -- I can't</p> <p>15 tell you. I'd have to look at the report, look</p> <p>16 at the analysis, to be able to give you a full</p> <p>17 and complete answer to that.</p> <p>18 Whatever it was we did that you're</p> <p>19 talking about, I'm almost certain it was done</p> <p>20 either in response to or in anticipation of</p> <p>21 what the plaintiffs would do in that -- what</p> <p>22 the plaintiff's expert would do in that report.</p> <p>23 And I think we were pretty clear</p> <p>24 that that's why we were doing it. I'm not</p> <p>25 sure.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 indicate which would be the most powerful tests</p> <p>3 to measure the relationship between trading and</p> <p>4 price change?</p> <p>5 A. I can't tell you without looking</p> <p>6 at a specific article.</p> <p>7 Q. Well, when you did your report,</p> <p>8 did you select different ways of determining</p> <p>9 the relationship between trading and price</p> <p>10 changes?</p> <p>11 A. Yes, we did.</p> <p>12 Q. But you didn't go back and look at</p> <p>13 the literature to see what they had to say</p> <p>14 about that?</p> <p>15 A. I did it based on my understanding</p> <p>16 of the appropriate way to conduct an</p> <p>17 investigation about whether an event, whether</p> <p>18 it be a news announcement or a trading, trade,</p> <p>19 occurred and what impact that had on the price.</p> <p>20 Q. Well, but you didn't -- you didn't</p> <p>21 go back and look at the literature to determine</p> <p>22 which one -- which measure or variable would be</p> <p>23 the more powerful variable to consider in</p> <p>24 determining the impact of trading on prices?</p> <p>25 A. I don't think there is a most</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 powerful variable. I think it depends on the</p> <p>3 facts and circumstances of the case, the</p> <p>4 trading, the firm, exchange the firm trades on,</p> <p>5 liquidity of the stock. Lots of things.</p> <p>6 And, so, that's why I think you</p> <p>7 need to look at a variety of different measures</p> <p>8 of potential trading activity.</p> <p>9 Q. Well, if you look at -- let's</p> <p>10 take that and let's look at a couple of</p> <p>11 examples.</p> <p>12 If you're looking at the trading</p> <p>13 to try to determine what impact trading had in</p> <p>14 December of 2009, between December 1st, 2009</p> <p>15 and December 10th, 2009, would it be</p> <p>16 appropriate to look at the trading that</p> <p>17 occurred in January two thousand -- January 1,</p> <p>18 2007 and January 31st of 2007?</p> <p>19 MR. SOHN: Can we -- can you just</p> <p>20 read that back so we can make sure we're all</p> <p>21 together?</p> <p>22 (Whereupon, the record is read</p> <p>23 back.)</p> <p>24 A. It depends on what -- overall what</p> <p>25 big-picture question you're trying to answer.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, that's an incomplete</p> <p>3 hypothetical. What's the question you're</p> <p>4 trying to answer?</p> <p>5 Q. I asked you is it relevant --</p> <p>6 A. Whose trades are you looking at</p> <p>7 and what's the purpose of the analysis?</p> <p>8 Q. Well, the purpose -- I'll give you</p> <p>9 the purpose of the analysis. To determine</p> <p>10 whether or not the trading that occurred by "X"</p> <p>11 in -- between December 1st, 2009 and December</p> <p>12 31st of 2009, and you're trying to determine</p> <p>13 what the impact of that trading was during that</p> <p>14 time period.</p> <p>15 Is the time period of what that</p> <p>16 person did on January 1, 2007 through January</p> <p>17 31st, 2007 relevant?</p> <p>18 MR. SOHN: I'm going to object to</p> <p>19 the form of the question, and it's been asked</p> <p>20 and answered.</p> <p>21 A. Yes, it's relevant. If you're</p> <p>22 trying to determine whether an entity "X" had</p> <p>23 an impact on the price in December, you</p> <p>24 certainly want to look at December. But if "X"</p> <p>25 is also trading in the stock other months, you</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 If you're trying to answer the question that</p> <p>3 we're trying to answer in this case, I think</p> <p>4 you need to look at the -- one of the things</p> <p>5 you need to look at is the entire trading range</p> <p>6 of the defendant, all the dates that he traded,</p> <p>7 to understand what, if any, price impact there</p> <p>8 is as a result of those trades.</p> <p>9 Q. I'm sorry, I didn't ask you about</p> <p>10 this case. I asked you a hypothetical.</p> <p>11 A. And I replied saying it depends,</p> <p>12 and gave you an example of how it might vary.</p> <p>13 And this is a case in how it might be</p> <p>14 important.</p> <p>15 Q. No, you just said that you</p> <p>16 concluded this case is of some importance. I</p> <p>17 think is your answer. Now, the question --</p> <p>18 A. Right.</p> <p>19 Q. Excuse me.</p> <p>20 My question, okay, is is it</p> <p>21 relevant what happened in my hypothetical in</p> <p>22 January 1, 2007 -- between January 1, 2007 and</p> <p>23 January 31st of 2007 in terms of determining</p> <p>24 what the impact of trading was on December 1st,</p> <p>25 2009 through December 31st of 2009?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 want to ask yourself, well, did it have an</p> <p>3 impact in those other months? And if it</p> <p>4 didn't, why am I finding -- why -- that may</p> <p>5 influence how you're looking at December. Or</p> <p>6 if it did, that may also influence on how</p> <p>7 you're looking at December.</p> <p>8 Q. Okay. So that's not -- that's --</p> <p>9 A. So I think if you're looking at an</p> <p>10 entity impact on a stock, entity's trades, you</p> <p>11 need to look at all of their trades.</p> <p>12 Q. Well, when you're looking at --</p> <p>13 you're taking "X," using my hypothetical "X,"</p> <p>14 and we're using the early time period of '07</p> <p>15 and comparing to the later time period in '09,</p> <p>16 okay, and you indicated that what the person</p> <p>17 did in the earlier time period could be</p> <p>18 relevant to what he did in the later time</p> <p>19 period. Is that fair?</p> <p>20 A. Not only what he did, but what the</p> <p>21 impact was, whether there was an impact on the</p> <p>22 price.</p> <p>23 Q. Now, would it be important to know</p> <p>24 what his motivations were in those two time</p> <p>25 periods?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. It might be, but sometimes you</p> <p>3 don't know that.</p> <p>4 Q. Okay.</p> <p>5 A. I mean...</p> <p>6 Q. Well, but is motivation an</p> <p>7 important factor to determine whether or not</p> <p>8 the model you developed is relevant?</p> <p>9 A. It might be.</p> <p>10 Q. Did you try to determine what the</p> <p>11 motivation was here?</p> <p>12 A. We weren't asked to determine</p> <p>13 intent. We were asked to look at the data to</p> <p>14 understand what the data told us about what the</p> <p>15 price impact was and to objectively look at the</p> <p>16 trading strategy and understand whether that</p> <p>17 was a legitimate optimal-type trading strategy</p> <p>18 to employ based on the characteristics of</p> <p>19 Sedona and based on the characteristics of the</p> <p>20 FPS.</p> <p>21 Q. Well, did you attempt to decide --</p> <p>22 to determine what the impact of buys were on</p> <p>23 prices?</p> <p>24 MR. SOHN: You're talking about</p> <p>25 this case now?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 nonparametric tests and the regression</p> <p>3 analysis -- what tests to run and what</p> <p>4 specifications to run.</p> <p>5 Q. Okay. Well, let's take Regression</p> <p>6 Number 1.</p> <p>7 Do you have the report in front of</p> <p>8 you?</p> <p>9 A. Yes.</p> <p>10 Q. Look at 13B, Exhibit 13B.</p> <p>11 Do you have that in front of you?</p> <p>12 A. Sorry?</p> <p>13 Q. Do you have that in front of</p> <p>14 you?</p> <p>15 A. I didn't say.</p> <p>16 Q. What is -- what -- what is the</p> <p>17 variable, the independent variable, for</p> <p>18 Regression Number 1?</p> <p>19 A. There are two independent</p> <p>20 variables: One is the NASDAQ return, and one</p> <p>21 is any Rhino open market trade.</p> <p>22 Q. What do you mean by "open market</p> <p>23 trade"?</p> <p>24 A. A buy or a -- a trade. A buy or a</p> <p>25 sell.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 MR. GUIDO: This case.</p> <p>3 A. Yes.</p> <p>4 Q. Did you measure it against bid-ask</p> <p>5 prices?</p> <p>6 A. No.</p> <p>7 Q. Did you determine what -- did you</p> <p>8 attempt to determine what the impact of sells</p> <p>9 were in this case?</p> <p>10 A. Yes.</p> <p>11 Q. Did you attempt to determine</p> <p>12 whether the sells were at the ask? I'm sorry,</p> <p>13 at the bid. Excuse me.</p> <p>14 A. We looked at the impact of buys</p> <p>15 and sells on the stock price.</p> <p>16 Q. Okay. But you didn't look to see</p> <p>17 whether or not the buys and sells were the bid</p> <p>18 or the ask?</p> <p>19 A. I believe we did not.</p> <p>20 Q. Who selected the variables for the</p> <p>21 various regressions that were included in the</p> <p>22 expert report?</p> <p>23 A. Tsvetan Beloreshki -- Beloreshki</p> <p>24 and I jointly agreed that, for all of our</p> <p>25 statistical tests -- the parametric tests,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. A buy or a sell.</p> <p>3 So any time there was a buy or a</p> <p>4 sell, you indicate a buy one; and if there</p> <p>5 wasn't, it was a zero. Is that correct?</p> <p>6 A. Right. And that's excluding</p> <p>7 direct purchases, conversions, transfers,</p> <p>8 things like that.</p> <p>9 Q. Okay. And what about the second</p> <p>10 regression? What was the independent variable</p> <p>11 there, or variables?</p> <p>12 A. Regression Number 2, there were</p> <p>13 three independent variables.</p> <p>14 Q. Okay.</p> <p>15 A. The NASDAQ return, Rhino purchases</p> <p>16 and, thirdly, Rhino sales.</p> <p>17 Q. And those are open market sales</p> <p>18 and purchases?</p> <p>19 A. Correct.</p> <p>20 Q. And those are transactions</p> <p>21 reported to the market?</p> <p>22 A. I believe so, yes.</p> <p>23 Q. Okay. And the third regression,</p> <p>24 what were the independent variables there?</p> <p>25 A. There were five independent</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 variables.</p> <p>3 Q. Okay. And what were those?</p> <p>4 A. The NASDAQ return, Rhino</p> <p>5 purchases, Rhino sales, transfers between Rhino</p> <p>6 accounts, and principal transactions which are</p> <p>7 either conversions or direct purchases of stock</p> <p>8 from Sedona.</p> <p>9 Q. And that's -- is that the fourth?</p> <p>10 I mean is that the third? I'm sorry.</p> <p>11 A. That's the third regression.</p> <p>12 Q. The third regression. Okay.</p> <p>13 A. Yes.</p> <p>14 Q. Now, in that regression, were</p> <p>15 there transfers reported to the market?</p> <p>16 A. I don't -- I don't believe they</p> <p>17 were.</p> <p>18 Q. Okay. Well, did you go out and</p> <p>19 attempt to ascertain whether they were reported</p> <p>20 to the market?</p> <p>21 A. We didn't determine that. It</p> <p>22 wasn't relevant to our analysis.</p> <p>23 Q. And what about the principal?</p> <p>24 What are those?</p> <p>25 A. As I said before, those were</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 were here?</p> <p>3 A. The number of shares?</p> <p>4 Q. The number of shares that were</p> <p>5 transferred -- transfers or principals in the</p> <p>6 data that you looked at.</p> <p>7 A. No, not -- not sitting here off</p> <p>8 the top of my head. I could look at the data</p> <p>9 and tell you just by adding them up.</p> <p>10 Q. Well, do you have any charts that</p> <p>11 indicate whether that -- whether you considered</p> <p>12 that variable in your report as an exhibit to</p> <p>13 your report?</p> <p>14 MR. SOHN: Objection to form.</p> <p>15 A. What variable?</p> <p>16 Q. The size of the transfers in terms</p> <p>17 of number of shares to the size of the</p> <p>18 principals compared to the number of shares.</p> <p>19 A. That regression is not reported</p> <p>20 here, but I believe that that is one of the</p> <p>21 variables we ran in one of our regressions.</p> <p>22 Q. Well, you believe or you reviewed</p> <p>23 it before you signed that report?</p> <p>24 A. I don't understand your question.</p> <p>25 Q. Well, I mean, I'm asking you what</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 either conversions of the FPS into Sedona stock</p> <p>3 or direct purchases of Sedona stock by Rhino.</p> <p>4 Q. And this is the time period May</p> <p>5 1st through May 31st. Is that correct?</p> <p>6 A. No.</p> <p>7 Q. Are you looking at 13B or 13A?</p> <p>8 A. I'm looking at 13B.</p> <p>9 Q. What's the time period?</p> <p>10 A. The time period is March 1st, 2001</p> <p>11 through May 31st, 2001.</p> <p>12 Q. During that time period.</p> <p>13 Do you know what the -- the number</p> <p>14 of transfers in terms of shares and the number</p> <p>15 of principals and conversions of nonmarket</p> <p>16 transactions were during that time period?</p> <p>17 A. I know there were a number of</p> <p>18 conversions. Four or five at least, probably;</p> <p>19 maybe more. There may have been a direct</p> <p>20 purchase of stock in there, as well. I don't</p> <p>21 know off the top of my head.</p> <p>22 And I couldn't tell you without</p> <p>23 looking at the data how many transfers were in</p> <p>24 that period.</p> <p>25 Q. So you don't know what the numbers</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 you did. I'm not asking you what you believe.</p> <p>3 A. I'm -- I'm saying that we ran a</p> <p>4 number of regressions. Four are reported here.</p> <p>5 In one of those other -- these are just flags.</p> <p>6 Okay? Zero/ones. So they don't count the</p> <p>7 number of shares.</p> <p>8 But I believe one of the other</p> <p>9 regressions that we ran counted the number of</p> <p>10 shares involved in transfers and principal.</p> <p>11 Q. No, but did you ever determine</p> <p>12 what the magnitude of the transfers in the</p> <p>13 principals were in relationship to the other</p> <p>14 transactions that were engaged in by Badian in</p> <p>15 this case? You refer to Badian as Rhino.</p> <p>16 A. We didn't do that specific</p> <p>17 calculation. That's easily done just by</p> <p>18 looking at the data.</p> <p>19 Q. You didn't do that, did you?</p> <p>20 A. We didn't do the specific</p> <p>21 calculation, but it basically is inherent in</p> <p>22 the data.</p> <p>23 Q. Well, I mean -- I mean, is it</p> <p>24 relevant what the size is in terms of the</p> <p>25 total number of transactions that you're</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 considering --</p> <p>3 MR. SOHN: Objection to form.</p> <p>4 Q. -- whether it's principal and</p> <p>5 transfers as opposed to open market sales?</p> <p>6 A. Well, if it's relevant, it will</p> <p>7 show up in the regression results in terms of</p> <p>8 having a price impact.</p> <p>9 Q. Or not having one.</p> <p>10 A. Exactly. And that will tell you</p> <p>11 whether it's relevant or not.</p> <p>12 Q. Well, if a transaction is not</p> <p>13 reported to the market, how does that have a</p> <p>14 price impact?</p> <p>15 A. There -- it could easily have a</p> <p>16 price impact. Just the information that</p> <p>17 someone has converted is important information</p> <p>18 for investors in that firm. That's a big</p> <p>19 event. That means that the person that's</p> <p>20 converted has a large number of shares, which</p> <p>21 if he hasn't -- if he hasn't shorted them</p> <p>22 earlier, that's important information that an</p> <p>23 investor might like to know.</p> <p>24 And, so it's quite, quite</p> <p>25 legitimate to test to see whether a non -- an</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. -- that other investors might</p> <p>3 obtain by virtue of knowing that a</p> <p>4 conversion happened --</p> <p>5 Q. Do you --</p> <p>6 MR. SOHN: Mr. Guido.</p> <p>7 MR. GUIDO: I'm sorry.</p> <p>8 A. -- or a direct purchase happened.</p> <p>9 Q. So you included in your analysis</p> <p>10 conversions and transfers, although you didn't</p> <p>11 know whether or not they were -- that</p> <p>12 information was available to the market at the</p> <p>13 time?</p> <p>14 A. We didn't do a study to determine</p> <p>15 that, but that's a complete and legitimate</p> <p>16 channel through which price might be affected.</p> <p>17 And, so, we wanted to test that.</p> <p>18 Q. Well, what's -- what has to happen</p> <p>19 before it has an impact?</p> <p>20 A. I've already told you.</p> <p>21 Q. It's available to the market.</p> <p>22 Right?</p> <p>23 A. The information -- if the</p> <p>24 information of a conversion or a direct</p> <p>25 purchase becomes available to the market,</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 off-market transaction might have an impact on</p> <p>3 the stock through that information.</p> <p>4 Q. Well, did you -- did you try and</p> <p>5 determine whether or not that information was</p> <p>6 available to the market? Conversions.</p> <p>7 A. We didn't -- we didn't determine</p> <p>8 whether the information was available to the</p> <p>9 market or not. We tested in our regression</p> <p>10 whether that channel of information might have</p> <p>11 had an impact.</p> <p>12 Q. Okay. But you don't know whether</p> <p>13 or not it was reported to the market?</p> <p>14 A. I don't know. I don't know</p> <p>15 whether the market became aware of the</p> <p>16 conversion soon after it happened.</p> <p>17 Q. Okay.</p> <p>18 A. But --</p> <p>19 Q. But is it important for the market</p> <p>20 to be aware of the transaction to measure it as</p> <p>21 having an impact on price of Sedona stock?</p> <p>22 A. Well, that's the channel through</p> <p>23 which the price might be impacted, is the</p> <p>24 information that other --</p> <p>25 Q. You didn't --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 that's important information. It's documented</p> <p>3 in the economic literature that issuance of</p> <p>4 stock is important information to investors.</p> <p>5 And if other investors become aware of it, then</p> <p>6 that's important information that may have an</p> <p>7 impact on the price.</p> <p>8 Q. Now, I think there's one more</p> <p>9 regression that's reported here?</p> <p>10 A. There's Regression Number 4 in</p> <p>11 Exhibit 13B.</p> <p>12 Q. Okay. And what were the variables</p> <p>13 that were included there?</p> <p>14 A. There were two independent</p> <p>15 variables: The NASDAQ return, and net daily</p> <p>16 shares transacted as a percent of total</p> <p>17 reported trading volume.</p> <p>18 Q. So there were three: NASDAQ, net</p> <p>19 transactions, and the market volume. Is that</p> <p>20 right?</p> <p>21 A. No, there are two independent</p> <p>22 variables. There are three pieces of</p> <p>23 information that go into those variables.</p> <p>24 Q. Okay.</p> <p>25 A. One is the NASDAQ return; and the</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 other two, which go into one variable, are net</p> <p>3 daily shares transacted as a percent of total</p> <p>4 reported trading volume.</p> <p>5 Q. Okay. And -- and -- what -- what</p> <p>6 went into determining the net transactions?</p> <p>7 A. Net daily shares transacted was</p> <p>8 just the net -- the net of buys and sells.</p> <p>9 Q. Buys and sells or buys, sells,</p> <p>10 transfers and --</p> <p>11 A. Buys and sells.</p> <p>12 Q. Just buys and sells?</p> <p>13 A. Buys and sells.</p> <p>14 Q. Not transfers and not principal --</p> <p>15 A. Not transfers, not principal. We</p> <p>16 ran another regression that included those.</p> <p>17 Q. Now, which one of the two is</p> <p>18 included in Exhibit 13B?</p> <p>19 A. Regression number 4 is -- one of</p> <p>20 the independent variables in Regression Number</p> <p>21 4, the numerator of that variable is net daily</p> <p>22 shares transacted. Net daily shares transacted</p> <p>23 is computed as buys minus sells as I previously</p> <p>24 defined buys and sells.</p> <p>25 Q. I'd like you to take a look at a</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 if I give the witness this version? It's a</p> <p>3 little better. Maybe he could see it easier.</p> <p>4 MR. GUIDO: That's fine.</p> <p>5 MR. SOHN: Okay.</p> <p>6 MR. GUIDO: I'm sorry, but the</p> <p>7 court reporter condensed it.</p> <p>8 MR. SOHN: Yeah.</p> <p>9 A. Yeah, I think I'm -- I think I'm</p> <p>10 there.</p> <p>11 Q. Okay.</p> <p>12 A. Well, there are a large number of</p> <p>13 sheets with AS -- columns AS through A --</p> <p>14 Q. Yeah, I mean, but -- but I'm --</p> <p>15 what I want you to look at is the first -- or</p> <p>16 the first of the sheets that have AS through</p> <p>17 AW, because it has the calculations at the top</p> <p>18 of it, of this sheet.</p> <p>19 A. Okay. I think I'm there.</p> <p>20 Q. Now, it has -- in AS it says</p> <p>21 "Regression 4," and in AV it says "Regression</p> <p>22 5A."</p> <p>23 Do you see that?</p> <p>24 A. No.</p> <p>25 Q. I mean 4A. Excuse me.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 document that has been marked as Exhibit No.</p> <p>3 14.</p> <p>4 MR. SCHECHTMAN: I'm sorry, what</p> <p>5 number did you say?</p> <p>6 MR. GUIDO: Fourteen.</p> <p>7 MR. SCHECHTMAN: Fourteen?</p> <p>8 MR. GUIDO: Yes, Deposition</p> <p>9 Exhibit No. 14. I had put a Tab 13B on it from</p> <p>10 BP-04. And as I explained to Mr. Sohn</p> <p>11 yesterday, that if you look at B-4, this is</p> <p>12 really, I think, something called SDA -- SDAN.</p> <p>13 It is not 13B, but it's the backup for Exhibit</p> <p>14 13B.</p> <p>15 BY MR. GUIDO:</p> <p>16 Q. I want to direct your attention.</p> <p>17 Does that have -- at the top -- across the top</p> <p>18 there are columns, I think. Is that correct?</p> <p>19 It starts, I think, with "B" and then it moves</p> <p>20 on --</p> <p>21 A. Yes.</p> <p>22 Q. I'd particularly like to address</p> <p>23 your attention to the second set which is -- I</p> <p>24 think it's AU -- or it's AS through AW.</p> <p>25 MR. SOHN: Mr. Guido, do you mind</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I see that.</p> <p>3 Q. Okay. Now one of them says -- AT,</p> <p>4 it says "Net daily sales transacted as A</p> <p>5 percentage of volume." AT it says.</p> <p>6 In AW it says "Net trading as</p> <p>7 percentage of volume." Although your Exhibit</p> <p>8 13B in your report says, "Net daily shares</p> <p>9 transacted as a percent of the total reported</p> <p>10 trading volume."</p> <p>11 Which is which?</p> <p>12 A. I believe the results that are</p> <p>13 reported in Regression 4 are the results</p> <p>14 associated with the Regression 4A, net trading</p> <p>15 as a percent of volume.</p> <p>16 Q. Okay. And what's the "P" value</p> <p>17 there?</p> <p>18 A. Seven percent. 7.08 percent.</p> <p>19 Q. All right. And what percentage of</p> <p>20 significance is that?</p> <p>21 MR. SOHN: Objection to form.</p> <p>22 A. I don't understand your question.</p> <p>23 Q. Well, is it -- is it -- is it 92.9</p> <p>24 here?</p> <p>25 A. It's not significant --</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 significant at the 95 percent level, which is</p> <p>3 the level we used here.</p> <p>4 Q. But it is significant at the 90</p> <p>5 percent level if you use the 90 percent</p> <p>6 level?</p> <p>7 A. If you use the 90 percent level,</p> <p>8 yes, it is.</p> <p>9 Q. Okay. Have you used the 90</p> <p>10 percent level?</p> <p>11 A. I haven't used the 90 percent</p> <p>12 level. I've used the 95 percent level.</p> <p>13 Q. Did you use the 90 in Pet</p> <p>14 Quarters?</p> <p>15 A. I don't believe we used 90 in Pet</p> <p>16 Quarters for the variables of interest. We may</p> <p>17 have -- we may have talked about something</p> <p>18 being weakly significant at 90.</p> <p>19 Q. But you did talk about 90 percent</p> <p>20 significance level?</p> <p>21 A. You'd have to show me the Pet</p> <p>22 Quarters report.</p> <p>23 Q. Well, I'm just asking you what you</p> <p>24 know.</p> <p>25 A. And without looking at the report,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I believe -- let me turn to</p> <p>3 Exhibit 3. The way it's written here, we don't</p> <p>4 have a -- we don't have a journal associated</p> <p>5 with it, but I do believe it came out in a</p> <p>6 peer-reviewed journal. We may have been</p> <p>7 referring here to the working paper, but I do</p> <p>8 believe it did come out in a peer-reviewed</p> <p>9 journal.</p> <p>10 Q. What's the significance of</p> <p>11 something being in a peer-reviewed journal?</p> <p>12 A. It means it's been reviewed by --</p> <p>13 it's gone through a peer-review process.</p> <p>14 Q. What's the significance of that?</p> <p>15 A. It means it's gone -- gone through</p> <p>16 a peer-review process and it's been approved</p> <p>17 for publication because it's relevant and of</p> <p>18 interest to -- the editor thinks it's of</p> <p>19 relevance and of interest to the readers of the</p> <p>20 journal.</p> <p>21 Q. You've written peer-reviewed</p> <p>22 articles, haven't you?</p> <p>23 A. Yes.</p> <p>24 Q. And, in fact, you claim that it's</p> <p>25 a positive for your qualifications as an expert</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 I couldn't give you the specifics apart from</p> <p>3 what I've already given you.</p> <p>4 Q. You remember or you don't. Okay.</p> <p>5 Now, the -- this Exhibit 13B, from</p> <p>6 your testimony, you said it's not significant</p> <p>7 at the 95 percent level, but the</p> <p>8 significance -- if you use your calculations,</p> <p>9 the significance is 92.92 percent, is it not?</p> <p>10 MR. SOHN: Objection to the form.</p> <p>11 A. On a stand-alone basis, correct,</p> <p>12 but none of these regressions are significant</p> <p>13 after you apply the appropriate correction to</p> <p>14 them.</p> <p>15 Q. Well, we'll talk about that a</p> <p>16 little later.</p> <p>17 The -- now, I want to go back to</p> <p>18 the literature that you were aware of with</p> <p>19 regard to how the market performed.</p> <p>20 And I think you mentioned the</p> <p>21 market conditions. Excuse me. I think you --</p> <p>22 you mentioned one study that was -- that you</p> <p>23 reviewed. That's the Chaplinsky piece.</p> <p>24 Was that in a peer-reviewed</p> <p>25 journal?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 witness, do you not?</p> <p>3 A. I don't think I claim it as a</p> <p>4 positive. It's the truth, so I put it down.</p> <p>5 Q. Okay. Well, how tall are you?</p> <p>6 A. Six-three and three-quarters.</p> <p>7 Q. Okay. Do you put that down?</p> <p>8 A. No.</p> <p>9 Q. Okay. So you thought it was</p> <p>10 relevant that you put it -- that you published</p> <p>11 articles in peer-reviewed journals, didn't</p> <p>12 you?</p> <p>13 A. I did think it was relevant.</p> <p>14 Q. And the question is why you</p> <p>15 thought it was relevant.</p> <p>16 A. Because people would be interested</p> <p>17 to know that I've published in peer-reviewed</p> <p>18 journals.</p> <p>19 Q. And what's the significance of</p> <p>20 publishing in a peer-reviewed journal?</p> <p>21 MR. SOHN: Objection.</p> <p>22 A. That you have had articles</p> <p>23 published on relevant topics in peer-reviewed</p> <p>24 journals.</p> <p>25 Q. Okay. And -- and having an</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 article published in a peer-reviewed journal as</p> <p>3 opposed to nonpeer-reviewed journals indicates</p> <p>4 that it's more accepted in the scientific</p> <p>5 community?</p> <p>6 MR. SOHN: Objection to form.</p> <p>7 A. I believe -- I wouldn't agree with</p> <p>8 that the way you stated it. I mean, there are</p> <p>9 plenty of articles out there that are -- that</p> <p>10 may not have appeared in peer-reviewed</p> <p>11 journals, but are used. But generally going</p> <p>12 through a peer review process shows that your</p> <p>13 article has been deemed relevant and</p> <p>14 interesting.</p> <p>15 Q. And significant?</p> <p>16 A. Well, I don't know about</p> <p>17 significant. Relevant and interesting.</p> <p>18 Q. Okay. Now, have you published</p> <p>19 anything in any journals on micro -- market</p> <p>20 microstructure studies?</p> <p>21 A. I don't believe you would call any</p> <p>22 of the peer-reviewed analysis I've done,</p> <p>23 studies I've done, under the heading of market</p> <p>24 microstructure. I think we categorize them</p> <p>25 under the heading of how financial markets</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Excuse me. That's the next one</p> <p>3 above?</p> <p>4 A. That's the next one above.</p> <p>5 Q. Okay.</p> <p>6 A. Then, the next one above that, "An</p> <p>7 Economic Analysis of the Private Equity</p> <p>8 Market."</p> <p>9 Q. Okay.</p> <p>10 A. And then, the next one above that,</p> <p>11 "Innovation and Finance in High-Tech Firms."</p> <p>12 Q. Okay.</p> <p>13 A. Then, the next one above that,</p> <p>14 "Angel investors and the Market for Angel</p> <p>15 Investments."</p> <p>16 Those would all be articles that</p> <p>17 either touch on or focus specifically on the</p> <p>18 financial markets that are available to small,</p> <p>19 risky firms.</p> <p>20 Q. Okay. Do any of those --</p> <p>21 A. So there -- hang on. I'm not</p> <p>22 done. There are others.</p> <p>23 Q. I'm sorry.</p> <p>24 A. That topic may be touched on in</p> <p>25 the two articles at the bottom of the first</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 work, how financial instruments work. In</p> <p>3 particular, how financial markets work for</p> <p>4 small, risky firms like Sedona. I think that</p> <p>5 would be the cate -- category that I would</p> <p>6 place them under.</p> <p>7 Q. Well --</p> <p>8 A. Among other categories.</p> <p>9 Q. Well, take a look at your resume.</p> <p>10 Can you point out which one of those you're</p> <p>11 referring to?</p> <p>12 A. Well, there are a variety of</p> <p>13 articles that touch on or focus on how firms</p> <p>14 raise finance. In particular, how small, risky</p> <p>15 firms raise finance. Those would be the</p> <p>16 following: "Recent Developments in Corporate</p> <p>17 Finance," the last one on the list.</p> <p>18 Q. What was --</p> <p>19 A. The last one -- the last one on</p> <p>20 the list. I'm starting at -- I'm going -- I'm</p> <p>21 starting at the latest and moving forward.</p> <p>22 Q. Okay.</p> <p>23 A. The -- "A Look at America's</p> <p>24 Corporate Finance Markets; "The Economics of</p> <p>25 the Private Placement Market: A New Look."</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 page of Exhibit 1, "Corporate Finance and</p> <p>3 Governance in an International Perspective."</p> <p>4 And "Corporate Governance in Eastern Europe and</p> <p>5 Russia: The Role of Banks." May be touched on</p> <p>6 in "Alternative Models of Financial System</p> <p>7 Development," the one above that.</p> <p>8 There's two art -- three</p> <p>9 articles --</p> <p>10 Q. Excuse me, I'm sorry. I missed</p> <p>11 that last one. What was it?</p> <p>12 A. "Alternative Models of Financial</p> <p>13 System Development." It's third from the</p> <p>14 bottom.</p> <p>15 Q. Okay.</p> <p>16 A. Eight from the bottom, "Trends and</p> <p>17 Prospects in Venture and Angel Investments in</p> <p>18 New Media Companies."</p> <p>19 Q. Okay.</p> <p>20 A. The one above that, "Angel</p> <p>21 Investors and the Angel Capital Electronic</p> <p>22 Network."</p> <p>23 The one above that, "The Private</p> <p>24 Equity Market."</p> <p>25 And, again, those are all articles</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 that focus on the finan -- how the financial</p> <p>3 markets for small, risky firms behave; what the</p> <p>4 incentives are for providers of finance and</p> <p>5 users of finance and how contracts are</p> <p>6 structured. Financial contracts are structured</p> <p>7 between the providers of finance and firms with</p> <p>8 regards to the types of securities that those</p> <p>9 small, risky firms will use.</p> <p>10 Then there is another article,</p> <p>11 "Dura's Impact on Damages," which doesn't talk</p> <p>12 about that -- that topic talks about event</p> <p>13 studies.</p> <p>14 Q. I think that what you just said is</p> <p>15 that these articles addressed how financial</p> <p>16 instruments are structured to raise capital for</p> <p>17 companies.</p> <p>18 Is that a fair characterization?</p> <p>19 A. No.</p> <p>20 Q. Okay.</p> <p>21 A. They either touch on or focus on</p> <p>22 how small firms that don't have access to, say,</p> <p>23 the corporate bond market or even the corporate</p> <p>24 equity market, how they raise finance. And the</p> <p>25 various different players in -- in the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 relative merits of different forms of</p> <p>3 financing?</p> <p>4 A. Well, we take -- we look at it</p> <p>5 from the point of view of economics, which --</p> <p>6 from a positive viewpoint as opposed to a</p> <p>7 normative viewpoint. We look at costs and</p> <p>8 benefits of different types of financing</p> <p>9 instruments. And we con -- we either imply or</p> <p>10 conclude that, you know, certain ways of</p> <p>11 raising finance for small, risky firms are just</p> <p>12 not possible because of the costs involved.</p> <p>13 The asymmetric -- asymmetric information costs,</p> <p>14 corporate control costs, other costs. Things</p> <p>15 like that.</p> <p>16 And, therefore, they are forced to</p> <p>17 go to other forms of finance such as the</p> <p>18 private equity market and the private debt</p> <p>19 market.</p> <p>20 Q. Okay. But the thrust of the --</p> <p>21 the thesis here is the benefits and cost of</p> <p>22 either going to the corporate bond market and</p> <p>23 the issuance of on-the-spot stock as opposed to</p> <p>24 privately negotiated instruments?</p> <p>25 A. I wouldn't say that's the focus.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 financial markets that they do have access to,</p> <p>3 such as the private equity markets, such as the</p> <p>4 private placement market.</p> <p>5 And the roles and incentives of</p> <p>6 the providers of finance and the -- the lenders</p> <p>7 and the users of finance, the firms, to -- how</p> <p>8 their -- how their incentives interplay to come</p> <p>9 up with the characteristics of the financial</p> <p>10 instruments that are actually used for the</p> <p>11 small firms to raise finance.</p> <p>12 Q. Do any of these articles address</p> <p>13 the benefits and costs to the -- the investors?</p> <p>14 A. Absolutely. They talk a lot about</p> <p>15 the structures that investors put in place to</p> <p>16 ensure that their -- they get a return on their</p> <p>17 money.</p> <p>18 Q. Do any of these address the</p> <p>19 benefits to the users for the issuance of these</p> <p>20 instruments?</p> <p>21 A. Absolutely. They talk about the</p> <p>22 benefits to the users of structuring contracts</p> <p>23 in particular ways in order to raise finance of</p> <p>24 most favorable terms.</p> <p>25 Q. Do any of these address the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 I'd say that was -- that's part of what was --</p> <p>3 I'd say the focus is on how exactly are the</p> <p>4 private equity markets and the private debt</p> <p>5 markets structured? What types of financial</p> <p>6 instruments do we see existing in those markets</p> <p>7 and why do we see them?</p> <p>8 Q. Okay. Did you --</p> <p>9 A. And that's based on the costs and</p> <p>10 benefits to the investors and the firms of</p> <p>11 entering into financial contracts with each</p> <p>12 other.</p> <p>13 (Cell phone ringing.)</p> <p>14 MR. GUIDO: Excuse me.</p> <p>15 We have to go off the record.</p> <p>16 Cellular phone.</p> <p>17 THE VIDEOGRAPHER: Going off the</p> <p>18 record at 11:10 a.m.</p> <p>19 (A recess is taken.)</p> <p>20 THE VIDEOGRAPHER: Going back on</p> <p>21 the record at 11:21 a.m.</p> <p>22 BY MR. GUIDO:</p> <p>23 Q. When we broke, I was asking you</p> <p>24 about your publications. And one of the</p> <p>25 questions I have for you is, do any of those</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 address the risks and benefits of future price</p> <p>3 securities to the issuer?</p> <p>4 A. Most of this work was done in the</p> <p>5 early '90s, before future price securities came</p> <p>6 on the scene, basically.</p> <p>7 Q. Okay.</p> <p>8 A. I think the studies tell us that</p> <p>9 the first future price securities were out</p> <p>10 there around 19 -- 1995. And while that was</p> <p>11 still a specialty of mine, small firm finance</p> <p>12 and how firms raise finance, I was very aware</p> <p>13 of future price securities around that time</p> <p>14 period, I don't believe a discussion of those</p> <p>15 got into any of these articles, with the one</p> <p>16 exception of the private equity market in the</p> <p>17 Handbook of Corporate Finance in 2002. I don't</p> <p>18 believe there's a discussion of FPS securities</p> <p>19 in there, but it's possible that there's a</p> <p>20 reference to them.</p> <p>21 But most of my articles were</p> <p>22 written in the early '90s, and the focus was on</p> <p>23 securities, you know, similar to FPS securities</p> <p>24 and the role they played in terms of giving</p> <p>25 firms access to finance that didn't have access</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 the concern was, well, where -- where do they</p> <p>3 go? Where do they go for finance?</p> <p>4 So there was an institutional</p> <p>5 motivation for me to be doing such research,</p> <p>6 but that was a research interest in and of</p> <p>7 itself by me.</p> <p>8 And, so, me and a group of others</p> <p>9 conducted an immense amount of research in that</p> <p>10 time period into the exact issues that, for</p> <p>11 example, Sedona would face in raising finance:</p> <p>12 Where do they go? How do they get it? What</p> <p>13 kinds of contracts could they construct with</p> <p>14 potential investors?</p> <p>15 And, so, there was -- and, so,</p> <p>16 there was definitely a -- a policy-oriented</p> <p>17 motivation, but there was also, just from a</p> <p>18 pure economics motivation, a desire to</p> <p>19 understand how do these markets work that we</p> <p>20 don't know much about that provide finance to</p> <p>21 small, risky firms like Sedona?</p> <p>22 Q. Okay. Thank you.</p> <p>23 Now, in any of these articles, did</p> <p>24 you address the question of market manipulation</p> <p>25 in future price securities?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 to other forms of finance, but didn't -- didn't</p> <p>3 specifically address FPS securities.</p> <p>4 Q. Well, I mean, a number of the</p> <p>5 papers, I think, that you indicated that you</p> <p>6 had written during that time period seem to</p> <p>7 have been written by -- at the time that you</p> <p>8 were at the Federal Reserve?</p> <p>9 A. Yes.</p> <p>10 Q. And were those papers that were</p> <p>11 intended to educate people on the various forms</p> <p>12 of financing that might be available to assist</p> <p>13 in economic development?</p> <p>14 A. That was part of it. The Fed is</p> <p>15 always interested in research on how firms</p> <p>16 raise finance, particularly those firms that</p> <p>17 don't have access to traditional forms of</p> <p>18 finance, like the corporate bond market and the</p> <p>19 corporate equity market.</p> <p>20 And particularly at this time</p> <p>21 period, we're in the credit crunch. And there</p> <p>22 was a very -- there was a very policy-oriented</p> <p>23 concern that, because of the credit crunch,</p> <p>24 firms -- small, risky firms, like Sedona, were</p> <p>25 getting shut out of traditional markets. And</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I don't believe we did.</p> <p>3 Q. Now, most of these articles are</p> <p>4 dated, it looks like, prior to 2000.</p> <p>5 A. Most of them. There's one in 2002</p> <p>6 and one in 2001.</p> <p>7 Q. Right.</p> <p>8 A. And one in 2000.</p> <p>9 Q. And there's one in 2008. Let's</p> <p>10 look at the one in 2008.</p> <p>11 Does that address the application</p> <p>12 of an event study to determine what damages are</p> <p>13 in a securities matter?</p> <p>14 A. Yes, specifically in a 10b-5</p> <p>15 matter.</p> <p>16 Q. Okay. And it's an allegation of</p> <p>17 fraud that you're --</p> <p>18 A. It's a.</p> <p>19 Q. -- talking about measuring in that</p> <p>20 article?</p> <p>21 A. An allegation that the firm made</p> <p>22 misrepresentations and omissions that investors</p> <p>23 would have found material.</p> <p>24 Q. And was that in a securities</p> <p>25 filing with the SEC?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Was what in a security --</p> <p>3 Q. What you were writing about.</p> <p>4 A. Well, we weren't writing about</p> <p>5 anything specific to the SEC. We were writing</p> <p>6 about what the proper method is to -- in using</p> <p>7 an event study to analyze the effect of a</p> <p>8 particular news -- a particular event such as a</p> <p>9 disclosure by a firm.</p> <p>10 Q. Well, what were the proper methods</p> <p>11 that you discussed in that paper to do event</p> <p>12 studies?</p> <p>13 A. Well, event study methodology is</p> <p>14 generally accepted in the economics literature</p> <p>15 and finance literature. And there's general</p> <p>16 accept -- I think there's general acceptance</p> <p>17 about how to go about doing an event study.</p> <p>18 There are, obviously, details about an event</p> <p>19 study that people may disagree about, but I</p> <p>20 think the overall approach to doing an event</p> <p>21 study is generally accepted.</p> <p>22 And we talked about that. And</p> <p>23 then, also, how the legal -- the legal</p> <p>24 environment affected -- or the changing legal</p> <p>25 environment affected the exact method by which</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 background market was that might have an effect</p> <p>3 on the particular stock price in your study.</p> <p>4 Is that one of the factors?</p> <p>5 A. That's one of the things that you</p> <p>6 look at to see how influential market and</p> <p>7 industry factors are on stock price movements</p> <p>8 of the company you're interested in.</p> <p>9 Q. Okay. And you said that you would</p> <p>10 focus on the particular event.</p> <p>11 What did you refer to when you</p> <p>12 said that?</p> <p>13 A. The particular event you're</p> <p>14 interested in in determining the price impact</p> <p>15 of. Whether it be a disclosure, whether it be</p> <p>16 some other event. That's what you want to look</p> <p>17 at.</p> <p>18 Q. Is it important that you pick the</p> <p>19 correct event to determine what the impact that</p> <p>20 event had on stock price?</p> <p>21 A. Well, if you know the event, I'm</p> <p>22 not sure there's an issue about picking the</p> <p>23 event. If you know the event that you're</p> <p>24 interested in studying, I'm not sure there's an</p> <p>25 issue about picking it. It's kind of a</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 you calculate damages in a shareholder class</p> <p>3 action using an event study, but also using</p> <p>4 other methods to calculate damages.</p> <p>5 Q. Well, what were the generally</p> <p>6 accepted methods that you addressed in that</p> <p>7 article that should be applied in the event</p> <p>8 study?</p> <p>9 A. We talked -- I think -- without</p> <p>10 having the article in front of me, I can't</p> <p>11 recall the exact details of what we talked</p> <p>12 about, but we talked about the fact that an</p> <p>13 event study is a generally accepted way to go</p> <p>14 about doing things.</p> <p>15 And I think we talked in general</p> <p>16 about how you go about doing an event study:</p> <p>17 You set up a market model; look at daily</p> <p>18 changes in stock returns; understand how stock</p> <p>19 returns vary with various market or industry</p> <p>20 indexes; and then, focus on the particular</p> <p>21 disclosures or events that you're interested in</p> <p>22 focusing on to identify whether there was a</p> <p>23 stock price impact due to those events.</p> <p>24 Q. So, in other words, in the market,</p> <p>25 you'd look to see -- you consider what the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 tautology. Once you determine what the event</p> <p>3 is, then you measure the impact of it.</p> <p>4 Q. Let me ask you, you used the term</p> <p>5 "market manipulation" in this report?</p> <p>6 A. Yes.</p> <p>7 Q. What do you mean by that?</p> <p>8 A. Well, I know there are legal</p> <p>9 definitions of market manipulation. And I'm</p> <p>10 not a lawyer. So I'm not -- I don't want to</p> <p>11 get -- I'm talking from an economics point of</p> <p>12 view, an economist's point of view. And I</p> <p>13 understand that one of the -- one of the</p> <p>14 aspects that you look at from an economics</p> <p>15 point of view in -- in determining overall</p> <p>16 whether or not there's been manipulation is</p> <p>17 whether there's been a price impact of the</p> <p>18 trades or other -- other transactions.</p> <p>19 So I understand that's one element</p> <p>20 in the ultimate legal judgment about whether</p> <p>21 there's been market manipulation or not.</p> <p>22 Q. No, I'm asking you how you used</p> <p>23 the term "market manipulation." It appears</p> <p>24 that -- in the very last paragraph of your</p> <p>25 expert report.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 How are you using that term?</p> <p>3 A. In my last paragraph?</p> <p>4 Q. Uh-huh. The one that -- the</p> <p>5 conclusion paragraph.</p> <p>6 A. Oh, that's the second to last</p> <p>7 paragraph.</p> <p>8 Q. I'm sorry.</p> <p>9 A. Right. The conclusion there comes</p> <p>10 from the analysis we have performed in the</p> <p>11 report, which shows a number of things: One,</p> <p>12 that Rhino pursued a legitimate strategy in</p> <p>13 trading Sedona stock given the riskiness of</p> <p>14 Sedona and giving the riskiness of the FPS</p> <p>15 security that it was holding.</p> <p>16 Two, that Sedona was an extremely</p> <p>17 risky company. Sedona knew it; investors knew</p> <p>18 it. And, so, investors had to react and hedge</p> <p>19 appropriately.</p> <p>20 And, also, the poor performance of</p> <p>21 Sedona shares over any time period can -- can</p> <p>22 be contrib -- can be explained by a lot of</p> <p>23 other fact -- a lot of factors that don't have</p> <p>24 anything to do with manipulation, such as the</p> <p>25 decline of the overall market, Sedona's</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 point in time Badian's trading hit the bid in</p> <p>3 the trading.</p> <p>4 You also testified that you didn't</p> <p>5 look to see whether or not Badian's purchases</p> <p>6 were at the offer.</p> <p>7 How can you determine whether or</p> <p>8 not something's a legitimate strategy unless</p> <p>9 you look to those two factors?</p> <p>10 MR. SOHN: Objection to form.</p> <p>11 A. I'm talking about the strategy</p> <p>12 that Rhino employed, because Sedona was an</p> <p>13 extremely risky company and the FPS was an</p> <p>14 extremely risky security, to short his position</p> <p>15 prior to conversion. That isn't -- on a broad</p> <p>16 level, overall level, that's an optimal</p> <p>17 strategy to pursue.</p> <p>18 Q. Okay. Let's take that --</p> <p>19 A. Because it -- because it minimizes</p> <p>20 your risks. And there are a lot of risks that</p> <p>21 you have to minimize.</p> <p>22 Q. Okay. Is it -- is it legitimate</p> <p>23 activity to violate a contract provision?</p> <p>24 A. That -- my understanding is that's</p> <p>25 not part of the SEC's -- that a violation, any</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 specific -- the decline in Sedona's industry,</p> <p>3 Sedona's peers, and Sedona-specific factors,</p> <p>4 such as, you know, it being a going concern, it</p> <p>5 never making any money. That type of thing.</p> <p>6 And then, finally, the economic or</p> <p>7 econometric and statistical analysis which</p> <p>8 fails to show any price impact of any kind --</p> <p>9 any kind of Rhino trading over any time period</p> <p>10 at all.</p> <p>11 Q. Okay. So, one of -- I mean, one</p> <p>12 component of your definition of market</p> <p>13 manipulation is that the econometrics failed to</p> <p>14 show a price impact?</p> <p>15 A. That's one component.</p> <p>16 Q. Okay.</p> <p>17 A. That's one component in our</p> <p>18 conclusion in paragraph 62.</p> <p>19 Q. And that the other components was</p> <p>20 that there was a -- there was a legitimate</p> <p>21 strategy --</p> <p>22 A. Correct.</p> <p>23 Q. -- that -- that was used here.</p> <p>24 Now, I think you said that you did</p> <p>25 not look to see whether or not at any given</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 violation of a contract is not part of the</p> <p>3 SEC's allegation, and we weren't asked to look</p> <p>4 at that.</p> <p>5 Q. No, I didn't ask you that</p> <p>6 question. I asked you the question whether</p> <p>7 violating a contract provision was a legitimate</p> <p>8 strategy.</p> <p>9 MR. SOHN: Objection to form.</p> <p>10 A. We weren't -- is that a</p> <p>11 hypothetical?</p> <p>12 Q. Yeah.</p> <p>13 A. What do you mean by "legitimate"?</p> <p>14 Q. I said, does violation of a</p> <p>15 contract provision constitute legitimate</p> <p>16 activity to you?</p> <p>17 MR. SOHN: Any contract provision?</p> <p>18 MR. GUIDO: Any.</p> <p>19 A. What do you mean by "legitimate"?</p> <p>20 Q. That -- you're the one who used</p> <p>21 the term. What do you mean by it?</p> <p>22 A. So are you using -- are you asking</p> <p>23 -- you --</p> <p>24 Q. I'm asking you.</p> <p>25 A. It's your hypothetical, though.</p>

18 (Pages 66 to 69)

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<p>1 - STEPHEN D. PROWSE - 2 So I just want to make sure that -- 3 Q. My hypothetical is using your term 4 "legitimate." 5 A. Okay. 6 Q. I'm asking whether or not within 7 your term "legitimate" includes violations of 8 contract terms. 9 MR. SOHN: Any contract terms? 10 MR. GUIDO: Any contract terms. 11 A. It may be if there's a dispute 12 over a contract and what a term means. One 13 firm -- one side may say you violated a 14 particular term. The other side may say, no, 15 we interpreted it this way. So there may be -- 16 there may be a dispute. 17 So it may be legit -- perfectly 18 legitimate from one firm's point of view if 19 they don't believe the contract provision means 20 what the other firm says it means. 21 Q. Take the hypothetical that there's 22 no question what the contract term means. 23 Is it legitimate to violate the 24 contract terms using your definition of 25 legitimate?</p>	<p>1 - STEPHEN D. PROWSE - 2 There may be disputes about issues like that. 3 So, you know, I can't answer your 4 hypothetical. 5 Q. Well, assume that there is no 6 dispute about the prohibition against shorting. 7 It's perfectly clear. There is no dispute 8 between the holder of the convertible debenture 9 and the issuer. They don't have a dispute 10 about it. Assume that. 11 Is a violation of that legit -- 12 that provision a legitimate activity in your 13 view, using your term "legitimate activity"? 14 MR. SOHN: Economic legitimate 15 activity. 16 MR. GUIDO: Just his term 17 "legitimate activity." You're the one who 18 added "economic." The witness said legitimate 19 activity. 20 A. Well, I said before, I'm not -- 21 I'm not a lawyer. So I'm not looking at, for 22 example, market manipulation terms in -- market 23 manipulation in legal terms. 24 So I'm going to answer your 25 question as an economist.</p>
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<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: So any unambiguous 3 contract terms? 4 MR. GUIDO: Any unambiguous 5 contract terms. 6 A. Well, it's hard for me -- in this 7 world it's hard for me to think of something 8 that's completely unambiguous to anybody, but 9 in your hypothetical it may be. It may be. 10 Q. Well, let me give you another 11 hypothetical, and we'll get closer to this 12 case. You have a contract provision that says 13 you may not short stock prior to submission of 14 a conversion letter. And the person holding 15 the convertible debenture shorts the stock 16 prior to submitting the conversion letter. 17 Is that legitimate activity in 18 your view? 19 MR. SOHN: Legitimate economic 20 activity? 21 MR. GUIDO: Yeah. 22 A. In your hypothetical, again, there 23 may be a dispute about the definition of 24 shorting. There may be a dispute about the 25 meaning of what was meant in the contract.</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. Okay. That's fine. 3 A. And there may be economic reasons 4 that are legitimate to violate a contract. 5 Q. Okay. 6 A. Violate a provision. 7 Q. Are there legitimate economic 8 terms (sic) to rob a bank? 9 A. Legitimate -- 10 MR. SOHN: Objection. 11 A. -- economic reasons? 12 Q. To rob a bank. 13 A. I doubt it because the risks are 14 just too high. 15 Q. Oh, because of the question of the 16 risks? 17 A. Yeah, because the risks are too 18 high of getting caught. 19 Q. So legitimacy in your view is 20 determined by what the risks are? 21 A. From an econo -- I'm saying from 22 an economic -- I'm not answering any of your 23 hypotheticals from a legal perspective. Okay? 24 I don't know what the law is regarding, in your 25 hypothetical, the violation of a particular</p>

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<p>1 - STEPHEN D. PROWSE - 2 provision. 3 From a -- from a purely economic 4 point of view -- and all economists will agree 5 with this. From a purely economic point of 6 view, you weigh the costs and benefits of doing 7 something. And if the benefits outweigh the 8 costs, then you do it. 9 Now, that is from a purely 10 economic point of view. It's taking law out of 11 it, although law might have a role in forming 12 the costs and benefits, and it's taking 13 morality out of it. So it's purely from an 14 economic point of view, weigh the costs and 15 benefits. And you say, how do I -- do I 16 benefit? 17 Q. So the cost and benefit is -- the 18 benefit is whatever the financial benefit is 19 and the cost is getting caught? 20 A. And the cost is whatever the 21 financial cost is. 22 Q. Including getting caught? 23 A. Including the risk of getting 24 caught maybe. 25 Q. And including getting put in jail?</p>	<p>1 - STEPHEN D. PROWSE - 2 law. 3 Q. Well -- 4 A. It recognizes the law. 5 Q. But you said you're not -- you're 6 not using the term "legitimate" in a legal 7 sense. 8 A. Except in your hypothetical when 9 you told me you'd go to -- when you rob a bank, 10 you go to jail. 11 Q. Now, the other point that you make 12 is that you looked at what their performance 13 was over time. 14 A. Yes. 15 Q. And that that affected your view 16 of whether the market was manipulated. 17 What was the time frame that you 18 were comparing? 19 A. We looked -- generally we looked 20 at two different time periods. We looked over 21 the entire time period of Rhino's trading, and 22 we looked at the period March 1st through May 23 31st, 2001. 24 Q. And you looked to see whether or 25 not the price declined over that time period?</p>
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<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: Objection. 3 A. Well, I'm not sure you get put in 4 jail for violating the provision of a 5 contract. 6 Q. No, but you do get put in jail for 7 robbing a bank, don't you? 8 A. If you get caught, I guess, yeah. 9 Q. I mean -- and that's why I gave 10 you the hypothetical. In terms of -- I'm 11 trying to understand how you're using the term 12 "legitimate activity." 13 So if -- so if -- I gather you're 14 saying is, is that irrespective of what the 15 contract provisions are or legal provisions 16 are, legitimate activity, in economic terms, 17 the way you're using it, is whether or not the 18 benefits outweigh the cost? 19 MR. SOHN: Objection to the form. 20 A. No, that's not true, because the 21 law has an element in forming what the costs 22 are. 23 Q. No, I understand that, but -- 24 A. So you said irrespective of 25 the law. Well, it's not irrespective of the</p>	<p>1 - STEPHEN D. PROWSE - 2 A. We looked to see what happened to 3 the price and what happened to other factors 4 that potentially could have affected that 5 price, such as the market, such as the 6 industry, such as Sedona-specific price -- 7 Sedona-specific events. 8 Q. Well, what events did you look 9 to? 10 A. Well, I can point some out in our 11 section on that. We looked at Section A. We 12 looked at market and industry peer group 13 factors. Section B we looked at Sedona -- 14 Q. I asked you about the 15 company-specific factors. 16 A. Okay. 17 Q. That's what I said. 18 A. Okay. And I'm turning to -- 19 Q. And I want to know what the 20 company-specific factors are that you looked to 21 in this study. 22 A. And page 9, Section B, is entitled 23 "Company-specific factors." 24 Q. Okay. Does it make reference to 25 any exhibit?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Let me look. Exhibit 7 and</p> <p>3 Exhibit 9 and Exhibit 8 are the exhibits that</p> <p>4 are referenced in that section. But there's</p> <p>5 also a lot of other information in the text</p> <p>6 that doesn't need an exhibit.</p> <p>7 Q. No, I understand that. But the</p> <p>8 "Company-specific factors," does it make</p> <p>9 reference to an exhibit in that section to</p> <p>10 support the statements about company-specific</p> <p>11 factors?</p> <p>12 A. And I've just told you that</p> <p>13 there are three exhibits referenced in that</p> <p>14 section.</p> <p>15 Q. Okay. Let's take a look at seven.</p> <p>16 A. But I want to make sure that</p> <p>17 that's not the only information -- I want to</p> <p>18 make sure you understand that that's not the</p> <p>19 only information we're relying on. We're</p> <p>20 relying on the entire section in the report</p> <p>21 which talks about a lot of other factors that</p> <p>22 are not in exhibits.</p> <p>23 Q. All right. With that</p> <p>24 qualification, take a look at Exhibit No. 8.</p> <p>25 A. Yes.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 company.</p> <p>3 I believe there's statistics in</p> <p>4 the Hillion and Vermaelen paper that says if</p> <p>5 you issue more than one FPS on average, there's</p> <p>6 a very high likelihood that you're going into</p> <p>7 bankruptcy in the next -- in the next year.</p> <p>8 Q. Is that just --</p> <p>9 A. And that is -- all this chart says</p> <p>10 is look at how many FPSs this company issued</p> <p>11 since its IPO. And, in particular, getting</p> <p>12 close to the issuance of the Series G in</p> <p>13 November 2000.</p> <p>14 This company was so risky it</p> <p>15 couldn't get money from anywhere.</p> <p>16 Q. So, therefore, it justified</p> <p>17 anything that Badian did to its stock. Is that</p> <p>18 your conclusion?</p> <p>19 A. No, that's not my conclusion at</p> <p>20 all. My conclusion is this company was</p> <p>21 extremely risky and -- by indication of its</p> <p>22 numerous issues of FPS securities. And,</p> <p>23 therefore, any investor buying those securities</p> <p>24 had better have a good strategy to hedge</p> <p>25 against those risks. Otherwise, he's going to</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. These are specific events. Right?</p> <p>3 A. Yes.</p> <p>4 Q. Did you do an event study on any</p> <p>5 of them?</p> <p>6 A. No, I did not.</p> <p>7 Q. In Pet Quarters, didn't you</p> <p>8 criticize the plaintiff's expert report because</p> <p>9 they pointed to company specific -- specific</p> <p>10 events and they failed to do event studies?</p> <p>11 A. You'd have to show me the specific</p> <p>12 section of the Pet Quarters report to remind me</p> <p>13 of that.</p> <p>14 Q. I --</p> <p>15 A. The point of this chart is not to</p> <p>16 do an event study on what happened to the stock</p> <p>17 price when a convertible issued. The point of</p> <p>18 this chart is to show that Sedona was a serial</p> <p>19 FPS issuer. This company couldn't raise money</p> <p>20 anywhere except through future price</p> <p>21 securities.</p> <p>22 That is a terrible indictment of</p> <p>23 the financial performance and the ability of</p> <p>24 that company to raise money, and is an</p> <p>25 indicator of the extreme riskiness of that</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 lose his shorts.</p> <p>3 Q. Even if he violates a contract</p> <p>4 provision? Assuming --</p> <p>5 A. I'm sorry, is there a question</p> <p>6 pending?</p> <p>7 Q. Assuming that there was a clear</p> <p>8 violation of the contract provision, is what</p> <p>9 you're saying is he better short the stock even</p> <p>10 if he's contractually agreed, clearly and</p> <p>11 unequivocally, not to do so? Is that your</p> <p>12 testimony?</p> <p>13 MR. SOHN: Is that a question?</p> <p>14 MR. GUIDO: That is a question.</p> <p>15 A. Well, now we're talking about this</p> <p>16 specific case and --</p> <p>17 Q. I --</p> <p>18 A. -- my -- and my understanding is</p> <p>19 that's not an allegation in the SEC --</p> <p>20 Q. I didn't ask you --</p> <p>21 A. It's not an allegation in the SEC</p> <p>22 complaint.</p> <p>23 Q. I didn't ask you whether it was an</p> <p>24 allegation in the complaint and that that's a</p> <p>25 legal judgment --</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well --</p> <p>3 Q. -- and you said you were not</p> <p>4 making legal judgments. Put the Complaint</p> <p>5 aside. I'm asking you a question about a fact,</p> <p>6 not about the Complaint.</p> <p>7 A. And what is the question?</p> <p>8 Q. And the question is: Does the</p> <p>9 condition of Sedona -- based on your statement</p> <p>10 about Chart 8 is an indictment of Sedona's</p> <p>11 performance, does that justify Badian violating</p> <p>12 a clear-cut contractual provision? Assuming</p> <p>13 it's clear-cut.</p> <p>14 MR. SOHN: Mr. Guido, two things:</p> <p>15 One, I'm going to object to your question; two,</p> <p>16 your voice is going up a little bit.</p> <p>17 MR. GUIDO: Well, I'm sorry, I'm</p> <p>18 trying to help the court reporter. She</p> <p>19 complained about my soft voice. Okay?</p> <p>20 MR. SOHN: We're going to work for</p> <p>21 a middle ground.</p> <p>22 A. And I have one clarification.</p> <p>23 It's not just Chart 8 that indicates the poor</p> <p>24 performance of Sedona. There's a lot of other</p> <p>25 charts in there.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 you want me to address?</p> <p>3 Q. I want you to answer, you know,</p> <p>4 whether or not it's a legitimate economic</p> <p>5 strategy as you've used the term. You've used</p> <p>6 the term.</p> <p>7 MR. SOHN: Objection.</p> <p>8 Q. So please answer the question</p> <p>9 based on your use of the term.</p> <p>10 A. Factoring in now your -- your</p> <p>11 assertion that this is a clear violation of the</p> <p>12 contract --</p> <p>13 Q. A contract provision.</p> <p>14 A. A contract provision?</p> <p>15 Q. That's correct.</p> <p>16 A. Well, it may be.</p> <p>17 Q. It may be?</p> <p>18 A. It may be a legitimate strategy.</p> <p>19 Q. Okay. Under what circumstances is</p> <p>20 it a legitimate strategy to violate a clear</p> <p>21 contractual term?</p> <p>22 MR. SOHN: Objection. This is</p> <p>23 like the tenth time that we've gone through</p> <p>24 this.</p> <p>25 A. Yeah, we weren't asked to address</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Okay.</p> <p>3 A. But, in addition, we weren't asked</p> <p>4 to address that issue. So I don't have an</p> <p>5 opinion on it.</p> <p>6 Q. Well, I mean, you -- you used --</p> <p>7 you used the term when I just asked you. You</p> <p>8 used the term "legitimate strategy." I'm just</p> <p>9 trying to find out what you're saying.</p> <p>10 A. And my -- my answer is that a</p> <p>11 legitimate strategy is an optimal strategy to</p> <p>12 hedge an FPS. And what we see Rhino doing is</p> <p>13 that optimal strategy.</p> <p>14 Q. Even if it's a violation of a</p> <p>15 clear-cut contractual provision?</p> <p>16 A. My understanding is that's not an</p> <p>17 issue in this case. And --</p> <p>18 Q. And --</p> <p>19 A. -- we specifically weren't asked</p> <p>20 to address it.</p> <p>21 Q. Okay. So now I'm asking you to</p> <p>22 address it.</p> <p>23 A. And --</p> <p>24 Q. You're the expert.</p> <p>25 A. And how do you want me -- what do</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 that issue and I can't give you an answer to</p> <p>3 all the conditions that would be in place.</p> <p>4 That's not something that we were asked to</p> <p>5 address as it's clear in our -- in our report.</p> <p>6 Q. Is there anywhere in your report</p> <p>7 where you indicate that you're not taking into</p> <p>8 consideration the contract terms?</p> <p>9 A. What is indicated in our report is</p> <p>10 the tasks we were asked to answer, the</p> <p>11 questions we were asked to answer.</p> <p>12 MR. GUIDO: Okay. Why don't we</p> <p>13 take a break. We'll get to the questions.</p> <p>14 THE VIDEOGRAPHER: This concludes</p> <p>15 Tape Number 1 in the videotaped deposition of</p> <p>16 Mr. Stephen Prowse. Going off the record at</p> <p>17 11:52 a.m.</p> <p>18 (A recess is taken.)</p> <p>19 THE VIDEOGRAPHER: This begins</p> <p>20 Tape Number 2 in the videotaped deposition of</p> <p>21 Mr. Stephen Prowse. Going back on the record</p> <p>22 at 12:01 p.m.</p> <p>23 BY MR. GUIDO:</p> <p>24 Q. Now, I think you testified before</p> <p>25 we went off the record that another one of the</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 factors that you considered in reaching your</p> <p>3 conclusion there was no more manipulation was</p> <p>4 that Sedona's performance over time explained</p> <p>5 by the market, the lack of the market, and the</p> <p>6 peers. Is that correct?</p> <p>7 A. Correct.</p> <p>8 Q. Okay. Did you do a statistical</p> <p>9 regression analysis against the new market</p> <p>10 indices?</p> <p>11 A. We did a regression analysis that</p> <p>12 included the NASDAQ as the -- one of the</p> <p>13 independent variables, correct.</p> <p>14 Q. Where -- where -- where in the</p> <p>15 exhibits can I find that?</p> <p>16 A. For example, Exhibit 13A.</p> <p>17 Q. Okay. And where is --</p> <p>18 A. Or 13B.</p> <p>19 Q. Pardon?</p> <p>20 A. Or 13B.</p> <p>21 Q. Or 13B or both?</p> <p>22 A. Or both.</p> <p>23 Q. Now, how can I tell looking at 13A</p> <p>24 whether there's a statistical significance of</p> <p>25 the relationship between Sedona stock and --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 happened to the NASDAQ stock price, in terms of</p> <p>3 a return, and then correlating the two through</p> <p>4 regression.</p> <p>5 Q. Okay. And in the correlating and</p> <p>6 through regression, do you average out those</p> <p>7 price changes over that time period to come up</p> <p>8 with a figure to compare it?</p> <p>9 A. No.</p> <p>10 Q. You use every day?</p> <p>11 A. It's a day-to-day comparison,</p> <p>12 correct.</p> <p>13 Q. All right. Now -- and it shows</p> <p>14 that there is a statistically significant</p> <p>15 relationship between the NASDAQ return and the</p> <p>16 Sedona return in 13A?</p> <p>17 A. It shows the "P" values are less</p> <p>18 than .01.</p> <p>19 Q. Okay. Which is 99 percent</p> <p>20 significant?</p> <p>21 A. That's -- that's looking at each</p> <p>22 regression on a stand-alone basis. Correct.</p> <p>23 Q. I understand.</p> <p>24 Now, take a look at 13B. That's</p> <p>25 March 1, 2001 through May 31st, 2009. The</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 stock price movement and NASDAQ's price</p> <p>3 movement?</p> <p>4 A. Well, if you were looking at these</p> <p>5 on a stand-alone basis, you'd look at the star</p> <p>6 indicators.</p> <p>7 Q. Okay. And that does -- under</p> <p>8 "NASDAQ return," does that double star denote a</p> <p>9 significance in the relationship between Sedona</p> <p>10 -- Sedona's stock price movement and NASDAQ</p> <p>11 price movement?</p> <p>12 A. Just looking at that one</p> <p>13 regression, the "P" value is greater than -- or</p> <p>14 less than .01.</p> <p>15 Q. Okay. So -- and -- so how -- I</p> <p>16 mean, how was that analysis done? What were</p> <p>17 the variables? Was it every day over this time</p> <p>18 period of June 26th 2000 to June 14th, 2002, or</p> <p>19 was it just the beginning and end time?</p> <p>20 A. No, it was daily data.</p> <p>21 Q. Daily data?</p> <p>22 A. So it was a regression analysis</p> <p>23 using however many trading days there are in</p> <p>24 that period, going from day to day, seeing what</p> <p>25 happened to Sedona's stock price, seeing what</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 NASDAQ return there doesn't have any asterisks.</p> <p>3 What does that signify?</p> <p>4 A. That signifies that the "P" value</p> <p>5 is greater than .05.</p> <p>6 Q. Okay. And does that indicate, in</p> <p>7 your opinion, that it lacks statistical</p> <p>8 significance?</p> <p>9 A. That's correct. It lacks</p> <p>10 statistical significance.</p> <p>11 Q. Now -- so that for the time period</p> <p>12 March 1 through May 31st, 2001, is it fair to</p> <p>13 conclude that you have not shown that Sedona's</p> <p>14 stock price was influenced by the NASDAQ</p> <p>15 return?</p> <p>16 A. You can't reject the hypothesis</p> <p>17 that the coefficient is zero.</p> <p>18 Q. Or that you can't reject the</p> <p>19 hypothesis that there's no relationship?</p> <p>20 A. You can't reject the hypothesis</p> <p>21 that there's no relationship.</p> <p>22 Q. Now, I'd like to also direct your</p> <p>23 attention to another exhibit which there was a</p> <p>24 -- that you chose to put in the exhibits and</p> <p>25 that is Exhibit 5A.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 I think you indicated that the --</p> <p>3 that the Sedona stock performance was an</p> <p>4 indictment of it and, therefore, it explained</p> <p>5 that any impact on its price was not due to</p> <p>6 market manipulation.</p> <p>7 And I'd like to direct your</p> <p>8 attention --</p> <p>9 A. No, I didn't say that.</p> <p>10 Q. I'm sorry. Well, you did give a</p> <p>11 quite lengthy response in which you did</p> <p>12 indicate that Sedona's stock -- stock price</p> <p>13 performance and its characteristics was an</p> <p>14 indictment, didn't you, of something?</p> <p>15 MR. SOHN: Objection.</p> <p>16 A. I said -- I said --</p> <p>17 Q. And what was that something?</p> <p>18 A. I said that its operating</p> <p>19 performance as -- and then as reflected, I</p> <p>20 believe, in its stock price volatility, its</p> <p>21 stock price decline, and -- and the fact that</p> <p>22 it relied almost solely on, or very largely on,</p> <p>23 FPS issues to raise money was indicative of it</p> <p>24 being a very risky stock.</p> <p>25 Q. Okay. Now, take a look at Exhibit</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, I don't have a color copy of</p> <p>3 the chart.</p> <p>4 MR. SOHN: [Handing document to</p> <p>5 witness.].</p> <p>6 A. Okay. So, Sedona is red. Well,</p> <p>7 it's hard to tell what it did without drawing</p> <p>8 lines on for the two dates you mentioned, which</p> <p>9 were March 1st and March 31st?</p> <p>10 Q. March 1st through May 31st.</p> <p>11 A. March 1st through May 31st. Okay.</p> <p>12 March 1st through May 31st. It looks like it</p> <p>13 went up, but -- overall, on average, but just</p> <p>14 eyeballing it, it doesn't look like it doubled</p> <p>15 to me.</p> <p>16 Q. Well, it did go from 20 to</p> <p>17 somewhere short of 40, didn't it?</p> <p>18 A. At some point in time, but I'm not</p> <p>19 sure where that is relative to May 31st.</p> <p>20 Q. Well, let me ask you something.</p> <p>21 You used the time period of June 26, 2000</p> <p>22 through June 14th, 2002, and you used March</p> <p>23 1st, 2001 through May 31, 2001, but -- for most</p> <p>24 of your other charts. But for some reason when</p> <p>25 you talk about stock price performance versus</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 5A. 5A, the Sedona price returns were in red.</p> <p>3 And look at the time period from -- the chart</p> <p>4 doesn't address the May 1 -- March 1 through</p> <p>5 May 31st, '01, but the chart seems to indicate</p> <p>6 that the price of Sedona during that period of</p> <p>7 time increased from a factor of about whatever</p> <p>8 this factor is on the left of 20 to somewhere</p> <p>9 just short of 40.</p> <p>10 What do those numbers mean on the</p> <p>11 left of this chart?</p> <p>12 A. These are -- this is just an</p> <p>13 index. So all the -- the three stock price</p> <p>14 indices -- the three stock price measures we're</p> <p>15 using here are all normalized to be the same on</p> <p>16 June 26, 2000.</p> <p>17 Q. Okay.</p> <p>18 A. And, so, basically you're</p> <p>19 comparing how the NASDAQ, Sedona and the peer</p> <p>20 group stock price performed since 2006 -- since</p> <p>21 June 26, 2000, relative to each other.</p> <p>22 Q. Okay. Well, does it indicate that</p> <p>23 the stock price of Sedona between March 1, 2001</p> <p>24 and May 31st, 2001, appears to have almost</p> <p>25 doubled in value?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 peer group companies and NASDAQ, you don't do</p> <p>3 it for that time period, do you?</p> <p>4 A. No, we don't.</p> <p>5 Q. Why not?</p> <p>6 A. I don't know. We talk -- I think</p> <p>7 we talk about it in the report. The report</p> <p>8 numbers are actually in the body of the report.</p> <p>9 Q. Where is that?</p> <p>10 A. But --</p> <p>11 Q. Where?</p> <p>12 A. Let me see.</p> <p>13 Q. Look at paragraph 37 in --</p> <p>14 A. Paragraph 37.</p> <p>15 Q. But that talks absolute prices.</p> <p>16 It doesn't talk about corrected prices, like</p> <p>17 you did for Exhibit 5A, does it?</p> <p>18 A. Well, I'm not sure what you mean</p> <p>19 by "corrected prices."</p> <p>20 Q. Well, you said that you</p> <p>21 normalized --</p> <p>22 A. Right, but that wouldn't change --</p> <p>23 that wouldn't change anything.</p> <p>24 Q. Okay. Well, it says --</p> <p>25 A. That wouldn't change anything.</p>

24 (Pages 90 to 93)

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Where is the data that supports</p> <p>3 paragraph 37?</p> <p>4 A. Well, the -- you have the data</p> <p>5 that supports paragraph 37.</p> <p>6 Q. Where is that?</p> <p>7 A. It's in the work sheets that were</p> <p>8 produced to you.</p> <p>9 Q. No, I mean in the report. In the</p> <p>10 report.</p> <p>11 A. Well, we didn't -- we didn't</p> <p>12 produce all of the data that support all the</p> <p>13 numbers in here. Most of the data's in the</p> <p>14 work sheets.</p> <p>15 Q. Really? Hmm.</p> <p>16 Now, --</p> <p>17 A. In fact, this data shows that the</p> <p>18 stock price declined over this period that you</p> <p>19 were talking about.</p> <p>20 Q. Well, then why did you put 5A in?</p> <p>21 What is the purpose of 5A, that shows an</p> <p>22 increase in the normalized -- or the adjusted</p> <p>23 back to 6/26/2000?</p> <p>24 A. I don't know. I'd have to look at</p> <p>25 the data -- I'd have to look at the data behind</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Yes.</p> <p>3 Q. Okay. Is this the -- the document</p> <p>4 that you relied upon to prepare Exhibit 13B in</p> <p>5 your expert report?</p> <p>6 A. I don't know where this comes</p> <p>7 from, 13 -- this exhibit.</p> <p>8 Q. Well, I'll represent to you it</p> <p>9 comes from a file called BP-4 and it's Tab</p> <p>10 13B.</p> <p>11 A. Okay.</p> <p>12 Q. In the documents that were</p> <p>13 produced by your office to the SEC.</p> <p>14 A. Okay.</p> <p>15 Q. Okay? Now, is that the document</p> <p>16 that you reviewed to prepare the 13B that is in</p> <p>17 your report?</p> <p>18 A. No, I didn't review this document.</p> <p>19 Q. Okay. Now, did you -- you know,</p> <p>20 when you did the report, okay, what did you</p> <p>21 review?</p> <p>22 A. What I --</p> <p>23 Q. In terms of data.</p> <p>24 A. In terms of data?</p> <p>25 Q. Uh-huh.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Exhibit 5A to understand what's going on, which</p> <p>3 is in the work sheets.</p> <p>4 Q. Do you know?</p> <p>5 A. And, you know, I made a decision</p> <p>6 not to -- not to include every single piece of</p> <p>7 analysis we did as an exhibit to the report.</p> <p>8 That would have been overkill. I would have</p> <p>9 had --</p> <p>10 Q. Overkill or data mining?</p> <p>11 A. No, it would have been overkill.</p> <p>12 Q. Now, --</p> <p>13 A. We didn't do any data mining.</p> <p>14 MR. GUIDO: I'd like to have</p> <p>15 marked as Exhibit No. 23 a rendition of Exhibit</p> <p>16 13B.</p> <p>17 MR. SOHN: Did you say "a</p> <p>18 rendition of"?</p> <p>19 MR. GUIDO: That's what I said,</p> <p>20 which is extracted from BP-4.</p> <p>21 (Whereupon, exhibit is received</p> <p>22 and marked BP-23 for identification.)</p> <p>23 BY MR. GUIDO:</p> <p>24 Q. Do you have Exhibit 23 in front of</p> <p>25 you?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I reviewed the exhibits as they</p> <p>3 were in -- as they were reported.</p> <p>4 Q. Okay.</p> <p>5 A. And I re -- and I had discussions</p> <p>6 with Erica Rose about the results of all the</p> <p>7 statistical analyses that we did on the Sedona</p> <p>8 matter.</p> <p>9 Q. Okay. And let's take the text of</p> <p>10 the report.</p> <p>11 Who wrote the initial draft?</p> <p>12 A. I believe the initial draft was</p> <p>13 written by Mr. Beloreshki. I'm not sure when.</p> <p>14 Prior to me getting involved in the -- in the</p> <p>15 engagement. But I took over the writing of the</p> <p>16 draft because, in November of 2009, we didn't</p> <p>17 have a whole lot of time to get the report out.</p> <p>18 And, so, I had -- I had spare time and</p> <p>19 Mr. Beloreshki didn't. So I took over,</p> <p>20 basically, the editing of the draft and the</p> <p>21 writing of the draft.</p> <p>22 Q. Well, take the second to the last</p> <p>23 paragraph in the -- in the report.</p> <p>24 Did you edit that paragraph?</p> <p>25 A. I can't remember. I can't</p>

25 (Pages 94 to 97)

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 remember if I edited it or not.</p> <p>3 Q. Well, when you edited the draft,</p> <p>4 did you review your edits with anyone?</p> <p>5 A. Did I review my edits?</p> <p>6 Q. Uh-huh.</p> <p>7 A. Mr. Beloroshki would have seen,</p> <p>8 and probably Erica would have seen, the final</p> <p>9 version before it went out, yes.</p> <p>10 Q. Well, from the day you got this</p> <p>11 draft and you started the editing process, who</p> <p>12 did you deal with about the draft?</p> <p>13 A. I dealt with Mr. Beloroshki and</p> <p>14 Erica Rose.</p> <p>15 Q. Anyone else?</p> <p>16 A. Perhaps we may have had a staff</p> <p>17 person in Dallas working on this, as well,</p> <p>18 Mr. Blanton.</p> <p>19 Q. Have you had a conversation with</p> <p>20 anyone from DLA Piper?</p> <p>21 A. Yes, we had conversations with DLA</p> <p>22 Piper.</p> <p>23 Q. And how often did you have these</p> <p>24 conversations?</p> <p>25 A. Specific to the draft?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 this case.</p> <p>3 Do you recall that?</p> <p>4 A. Yes.</p> <p>5 Q. In fact, it was served on you at</p> <p>6 home, right, as I recall?</p> <p>7 A. Actually, it was not served on me.</p> <p>8 It was served on my wife.</p> <p>9 Q. On your wife?</p> <p>10 A. And my older daughter.</p> <p>11 Q. And your older daughter.</p> <p>12 A. Who were upset.</p> <p>13 Q. Yeah, I understand that. I heard</p> <p>14 that.</p> <p>15 And were you aware that the</p> <p>16 subpoena had been -- a processor had attempted</p> <p>17 to serve you at your office as part of that?</p> <p>18 A. I can't remember. I was traveling</p> <p>19 most of that week, so I wasn't in the office.</p> <p>20 Q. Did you -- did you give</p> <p>21 instructions to the people in the office not to</p> <p>22 accept subpoenas for you when you were not</p> <p>23 there?</p> <p>24 A. I didn't give any instructions.</p> <p>25 Q. Well, do you have standard</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Uh-huh.</p> <p>3 A. Probably not many. Maybe one at</p> <p>4 the end; maybe two at the end. I believe we</p> <p>5 probably had a WebEx set up.</p> <p>6 Q. What's a WebEx?</p> <p>7 A. Where they can look at the</p> <p>8 draft -- they go into our -- we send them a</p> <p>9 link to our server. They go in, they click on</p> <p>10 the link and go in and can look at the draft.</p> <p>11 Q. Does that include red lines?</p> <p>12 A. Can they see red lines?</p> <p>13 Q. Does your WebEx include red lines?</p> <p>14 When a draft appears on that WebEx, does it</p> <p>15 include red lines?</p> <p>16 A. I don't know. If there are red</p> <p>17 lines -- it shows that -- it shows literally</p> <p>18 the report. So if the report has red lines in</p> <p>19 it at that point, then it -- then it will show</p> <p>20 them.</p> <p>21 Q. But when you did your edits, did</p> <p>22 you do them as red lines?</p> <p>23 A. I can't remember whether I did</p> <p>24 them or not. Probably.</p> <p>25 Q. Well, you received a subpoena in</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 instructions?</p> <p>3 A. No.</p> <p>4 Q. Do you --</p> <p>5 A. I very rarely receive -- receive</p> <p>6 subpoenas.</p> <p>7 Q. Now, when you received the</p> <p>8 subpoena, did you attempt to determine what</p> <p>9 you had in your files in response to that</p> <p>10 subpoena?</p> <p>11 A. Yes. I spoke with in-house</p> <p>12 counsel, spoke with DLA Piper, spoke with</p> <p>13 Erica, and I believe I spoke with Tsvetan, as</p> <p>14 well, and we produced what documents we were</p> <p>15 asked to produce.</p> <p>16 Q. When did you produce those?</p> <p>17 A. Soon after receiving the subpoena.</p> <p>18 I can't remember the exact date.</p> <p>19 Q. Who did you produce them to?</p> <p>20 A. I think we put them on a disk and</p> <p>21 sent them to DLA Piper.</p> <p>22 Q. Did you have any role in putting</p> <p>23 any documents on a disk yesterday?</p> <p>24 A. I had a role in that I instructed</p> <p>25 Mr. -- a person in my staff to put some</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 documents on a disk and send it as a response</p> <p>3 to a supplemental request, I guess, or</p> <p>4 something for something that we hadn't produced</p> <p>5 before that you wanted. So we put that</p> <p>6 together and sent you a disk, which I</p> <p>7 believe -- I'm not sure if you've gotten it</p> <p>8 yet. That was happening either the day before</p> <p>9 yesterday or yesterday.</p> <p>10 Q. Well, when you got the subpoena,</p> <p>11 did you pull together the documents that had</p> <p>12 been requested in that subpoena?</p> <p>13 A. Yes, I believe so.</p> <p>14 Q. And what did you do with the</p> <p>15 documents you pulled together after you</p> <p>16 received the subpoena?</p> <p>17 A. Put them on -- had them put on a</p> <p>18 disk and sent to DLA Piper.</p> <p>19 Q. Do you recall what the date was?</p> <p>20 A. No.</p> <p>21 Q. Was it shortly after you filed the</p> <p>22 report?</p> <p>23 A. It was shortly after I receive the</p> <p>24 subpoena.</p> <p>25 Q. Was it prior to the date you were</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 just skipped over Exhibit 22.</p> <p>3 MR. SOHN: I mean, 22 is</p> <p>4 available.</p> <p>5 THE REPORTER: Twenty-two -- 21 is</p> <p>6 here. We premarked 21 and 22. All right? So</p> <p>7 this is going to be another BP-22 then.</p> <p>8 (Whereupon, exhibit is received and</p> <p>9 marked BP-22 for identification.)</p> <p>10 MR. SOHN: Thank you.</p> <p>11 BY MR. GUIDO:</p> <p>12 Q. Do you recognize Exhibit 22 as the</p> <p>13 subpoena that was served upon you?</p> <p>14 A. It looks like it.</p> <p>15 Q. Okay. Now, it has a return date</p> <p>16 of December 11th on it.</p> <p>17 Do you see that?</p> <p>18 A. Correct.</p> <p>19 Q. Did you pull together the</p> <p>20 documents before December 11th?</p> <p>21 A. No, because -- I don't believe I</p> <p>22 did. I think December -- I can't remember. I</p> <p>23 think December 11th is -- it's either a Friday</p> <p>24 or Saturday, I believe. And I think I received</p> <p>25 the subpoena, or my wife and daughter received</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 ordered to produce the documents in the</p> <p>3 subpoena?</p> <p>4 MR. SOHN: Can we just be clear if</p> <p>5 we're talking about the order, you know, the</p> <p>6 evening order or the return date on the</p> <p>7 subpoena?</p> <p>8 MR. GUIDO: Yeah, I'm going to</p> <p>9 give you that right now. Thank you, Mr. Sohn.</p> <p>10 I'd like to have marked as an</p> <p>11 exhibit, next number, the subpoena that was</p> <p>12 serve on Mr. Prowse, or a copy of it.</p> <p>13 I think we originally talked about</p> <p>14 this as being Exhibit No. 23 when I talked to</p> <p>15 the --</p> <p>16 MR. SOHN: You just marked 23, so</p> <p>17 this should be 24.</p> <p>18 MR. GUIDO: So it now has to be</p> <p>19 24.</p> <p>20 THE REPORTER: We premarked this</p> <p>21 as Exhibit 23.</p> <p>22 MR. SOHN: Why --</p> <p>23 THE REPORTER: I mean, I'm sorry,</p> <p>24 we premarked this as Exhibit 22. So do you</p> <p>25 want to rename it as Exhibit 22? Because we</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 the subpoena on Thursday night. And I was not</p> <p>3 going to be in the office on Friday, so there</p> <p>4 was no way I could get the documents together</p> <p>5 in response to this subpoena.</p> <p>6 So I immediately called my in-house</p> <p>7 counsel, and they had, I believe, discussions</p> <p>8 with DLA Piper. And I think at some point the</p> <p>9 following week we produced the documents.</p> <p>10 Q. Now, the -- you testified, with</p> <p>11 regard to Exhibit 13B, the only rendition of</p> <p>12 13B that you saw was the one that's in your</p> <p>13 expert report, which is Deposition Exhibit 4.</p> <p>14 MR. GUIDO: Mr. Sohn, can you give</p> <p>15 the witness the copy of the expert report that</p> <p>16 has the color highlighted?</p> <p>17 MR. SOHN: Sure.</p> <p>18 BY MR. GUIDO:</p> <p>19 Q. Is Exhibit 13B from the</p> <p>20 Deposition Exhibit No. 4 your Exhibit No. 24,</p> <p>21 which was another rendition of Exhibit 13B? Is</p> <p>22 that the document that you reviewed?</p> <p>23 MR. SOHN: Mr. Guido, I think that</p> <p>24 it's Exhibit 23, not Exhibit 24.</p> <p>25 MR. GUIDO: Oh, excuse me.</p>

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<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: Is that right? 3 MR. GUIDO: Yes. 4 MR. SOHN: And I think you already 5 asked the question, but... 6 MR. GUIDO: Sorry. 7 BY MR. GUIDO: 8 Q. Which one of these did you review 9 when you signed the report? 10 A. When I signed the report, I 11 reviewed the one in the report. 12 Q. Okay. And any time after you were 13 retained to participate in drafting the report, 14 did you review Exhibit 23? 15 MR. SOHN: Objection. I think you 16 already asked that question. 17 A. I can't -- no, not that I can 18 remember. 19 MR. GUIDO: I'd like to have 20 marked as exhibit next number, if somebody 21 would please tell me what the number is. 22 THE REPORTER: Twenty-four. 23 MR. GUIDO: Twenty-four? Sorry. 24 (Whereupon, exhibit is received 25 and marked BP-24 for identification.)</p>	<p>1 - STEPHEN D. PROWSE - 2 done that? 3 MR. SOHN: Objection to form. 4 A. No. 5 Q. Did you discuss the regression 6 results for Regression No. 5 with anyone before 7 you signed the expert report No. 4, which is 8 Exhibit No. 4? 9 A. Yes, I discussed all the 10 regression results fairly early on in the 11 analysis because this analysis is fairly easy 12 to run once you have the data up and running, 13 which we did. So I discussed all of the 14 regression results with Erica Rose prior to 15 issuing the report. 16 Q. The -- you discussed it with Erica 17 Rose? 18 A. Yes, who is a staff person working 19 with me on this engagement. 20 Q. Okay. And what was your 21 discussions with Erica Rose about Regression 22 Number 5? 23 A. Well, she told me, again, fairly 24 early on in the engagement, that of all the 25 regressions she ran, she got "P" values of</p>
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<p>1 - STEPHEN D. PROWSE - 2 BY MR. GUIDO: 3 Q. Have you ever seen Exhibit 24 4 before? 5 A. I don't believe so, no. 6 Q. Do you know how Exhibit 23 -- 7 Exhibits 23 and 24 came to be produced? 8 A. I'm sure they were in -- in the 9 work sheets that we produced to you. 10 Q. Did you know that Exhibit No. 23 11 is the way the work sheet appeared in BP-4 when 12 it was opened and examined? 13 MR. SOHN: Objection to the form. 14 What is "it"? 15 A. No. 16 Q. Did you know that the Column T, 17 the numbers in the Column T, were omitted from 18 the sheet as it appeared in the spreadsheet 19 BP-04? 20 A. No. 21 MR. SOHN: Objection to form. 22 Q. Okay. Did you know that anyone 23 had applied the hidden function to that column? 24 A. No, I do not. 25 Q. So you don't know that anyone had</p>	<p>1 - STEPHEN D. PROWSE - 2 greater than .05 for all of them except for 3 two, I believe, which I believe is Regression 4 Number 5 and then one other. 5 Q. And that was Regression 4A, wasn't 6 it, initially? 7 A. I don't know what it was 8 originally. It's one -- it's the -- the other 9 one is the one that uses -- that doesn't use 10 the NASDAQ. It drops the NASDAQ out and uses 11 net daily share transacted. 12 Q. And that was the March 1st through 13 May 31st time period? 14 A. Correct. So she told me that out 15 of all the regressions she ran, she got a "P" 16 value greater than .05 on all of them except 17 for two. 18 And I made a mental note of that. 19 I thought, okay, I'm going to have to explain 20 in the report why these two regre -- or drop a 21 footnote and explain why these two regressions 22 don't change our opinion because of the correct 23 adjustment you have to make when you're making 24 multiple comparisons. 25 And I forgot to do that. I</p>

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<p>1 - STEPHEN D. PROWSE - 2 forgot to drop the footnote in the final 3 version of report to indicate that there were 4 regressions run that had "P" values of greater 5 than .05. 6 And the final decision to make -- 7 which regressions to display was made towards 8 the end of the engagement. And at that point I 9 had forgotten what Regression Number 5 -- the 10 results of Regression Number 5. And I 11 mistakenly and, unfortunately, told Erica just 12 report the first four, because I think they're 13 a fair representation of what -- of the 14 regressions we ran. 15 And I forgot to draw -- I forgot 16 to put a note in the report saying there were 17 other regressions we ran. Two of them had "P" 18 values greater than .05, but this doesn't 19 change our opinion because of the adjustment 20 you have to make. 21 So Regression Number 5 not being 22 included in the report was my fault, and I 23 apologize for that. 24 Q. All right. Take a look at -- 25 MR. GUIDO: Could you give the</p>	<p>1 - STEPHEN D. PROWSE - 2 included as exhibits, I had already determined 3 I wasn't going -- I wasn't going to show as an 4 exhibit every piece of analysis we'd already 5 done. 6 And, so, I decided -- I told Erica 7 just report the first four, because I think 8 that's a fair summary of what our regressions 9 are. And I forgot to put a note in the -- into 10 the report saying there were two other 11 regressions of the 18 we ran that had "P" 12 values of less than .05, but that that doesn't 13 change our opinion. 14 Q. Well, let me -- let me change the 15 subject a little bit before I go any further 16 with -- with this. 17 And that is this BE/BF column -- 18 forget the report. BE/BF. It doesn't -- it 19 doesn't describe that it's net daily trading 20 absent NASDAQ. 21 Why doesn't it have a description 22 on those columns of what those calculations 23 relate to? 24 A. I don't know why. 25 Q. Did you ever see it with the</p>
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<p>1 - STEPHEN D. PROWSE - 2 witness the larger rendition of Exhibit No. 4 3 to him? 4 MR. SCHECHTMAN: Is that this? 5 MR. SOHN: Yeah. 6 MR. GUIDO: It's what is referred 7 to as Tab 13B. 8 BY MR. GUIDO: 9 Q. I want you to take a look at the 10 very last page of this. 11 Are the columns BE and BF the 12 regression that is net daily trades excluding 13 NASDAQ? 14 A. Are you asking me is that what the 15 regression is? 16 Q. Yes. 17 A. I -- I believe it is. 18 Q. Okay. So that's one of the others 19 that you talked to Erica about excluding from 20 the report? 21 MR. SOHN: Objection to form. 22 A. No, I didn't talk to her about 23 excluding it from the report. If you remember, 24 what I said was when the time came to formulate 25 what exact statistical analysis would be</p>	<p>1 - STEPHEN D. PROWSE - 2 description? 3 A. No, I never saw -- I never saw 4 this data physically. I -- it was communicated 5 to me verbally what the results were. 6 Q. Because you never really looked at 7 the data itself. You have only had people tell 8 you verbally what the data showed. Isn't that 9 correct? 10 A. I've looked at the database that 11 we're using and I've looked at some of the 12 other results, but I didn't look at -- I 13 didn't go into the database and look at the 14 exact "P" values. They were communicated to me 15 verbally. 16 Q. So you -- you've never looked at 17 the document that's been marked as Exhibit No. 18 14? 19 A. Oh, I have. I have since issuing 20 the report, yes. 21 Q. Since issuing. But prior to 22 issuing your report, you didn't look at it, did 23 you? 24 A. I may have looked at the front 25 part of the data which had the stock prices on</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 them.</p> <p>3 Q. Uh-huh.</p> <p>4 A. But I don't remember going through</p> <p>5 each regression and looking at each one.</p> <p>6 Q. Now, in drafting the report -- let</p> <p>7 me see if I get this right -- you decided to</p> <p>8 exclude the regressions that showed a</p> <p>9 significant correlation to the 95 percent</p> <p>10 level?</p> <p>11 MR. SOHN: Objection to form.</p> <p>12 A. I decided to include the first</p> <p>13 four. And at the time I made that decision, I</p> <p>14 had forgotten that there were two regressions</p> <p>15 that had a "P" value of greater than point --</p> <p>16 of than less than .05 on them.</p> <p>17 Q. Now, let me ask you some</p> <p>18 questions.</p> <p>19 Have you ever been involved in</p> <p>20 accounting for a case measuring -- have you</p> <p>21 ever been involved in cases in which you've</p> <p>22 measured damages in a financial fraud or an</p> <p>23 accounting fraud case?</p> <p>24 A. Yes, I believe so.</p> <p>25 Q. And have you ever been involved in</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, let me ask the question a</p> <p>3 different way.</p> <p>4 Do you think it's a significant</p> <p>5 omission from your report that you do not</p> <p>6 address the other two regressions and explain</p> <p>7 why you thought that they were not significant</p> <p>8 for your conclusions?</p> <p>9 A. Yes, I do. It was a mistake and I</p> <p>10 should have noted it in the report that there</p> <p>11 was two regressions that we found that had "P"</p> <p>12 values of less than .05.</p> <p>13 Q. Now, I think you indicated that</p> <p>14 the last time that you read any literature on</p> <p>15 micro kept (sic) structure was when you got</p> <p>16 your study for your -- what is it, the FCA?</p> <p>17 When you studied for your Ph.D.</p> <p>18 A. That's actually not technically</p> <p>19 correct, no.</p> <p>20 Q. I'm sorry. I -- sometimes my</p> <p>21 memory fails me.</p> <p>22 When did you -- when did you study</p> <p>23 microstructures?</p> <p>24 A. I studied micro -- market</p> <p>25 microstructure as part of my Ph.D. training, as</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 one of those cases in which there was -- an</p> <p>3 allegation of fraud involved the destruction of</p> <p>4 work papers?</p> <p>5 A. Maybe.</p> <p>6 Q. Maybe.</p> <p>7 So you're aware that accountants</p> <p>8 are required to retain their work papers even</p> <p>9 if they don't support their conclusions?</p> <p>10 A. I'm not -- I'm not aware of what</p> <p>11 the exact accounting requirements are. I'm not</p> <p>12 an accountant.</p> <p>13 Q. Well, I mean, have you ever heard?</p> <p>14 I'm just asking if you ever heard.</p> <p>15 A. I have a general understanding</p> <p>16 that accountants need to keep their work</p> <p>17 papers.</p> <p>18 Q. And do you have a general</p> <p>19 understanding that at one point in time there</p> <p>20 was a debate about whether or not they had to</p> <p>21 keep their work papers that only supported</p> <p>22 their conclusions as opposed to all of their</p> <p>23 work papers that did not support their</p> <p>24 conclusions?</p> <p>25 A. I don't remember that.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 part of my CFA training. And in the time --</p> <p>3 and in those time -- so, in those time periods.</p> <p>4 Q. Now, in those time periods when</p> <p>5 you studied it, did you study about the</p> <p>6 importance of how you structured the model to</p> <p>7 reach conclusions based on regression</p> <p>8 analysis?</p> <p>9 MR. SOHN: Objection to form.</p> <p>10 A. I can't recall specifics. But, in</p> <p>11 general, structuring the model in any manner</p> <p>12 is -- is important.</p> <p>13 Q. And is it important that you have</p> <p>14 a certain degree of expertise in that field for</p> <p>15 which you were measuring the results in a</p> <p>16 regression analysis?</p> <p>17 MR. SOHN: Objection to form.</p> <p>18 A. Well, first of all, you have to</p> <p>19 have expertise in regression.</p> <p>20 Q. Okay.</p> <p>21 A. And, second of all, you have to</p> <p>22 have expertise in general in the area, the</p> <p>23 general area that you're looking at, whether it</p> <p>24 be financial economics, financial instruments,</p> <p>25 financial markets.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, is -- what is it about your</p> <p>3 background that makes you think that you're</p> <p>4 qualified to decide that two regressions that</p> <p>5 do not support your conclusions on their face</p> <p>6 should be excluded from your report?</p> <p>7 MR. SOHN: Objection to the form.</p> <p>8 A. Well, I've already testified that</p> <p>9 that was a mistake. And I would have -- and I</p> <p>10 had forgotten that there were "P" values</p> <p>11 associated with those two regressions that were</p> <p>12 less than .05.</p> <p>13 It doesn't -- my -- my</p> <p>14 qualifications as being an expert in regression</p> <p>15 or understanding what's significant and what's</p> <p>16 not are based on my training, my education, my</p> <p>17 skills, my knowledge. I've been doing</p> <p>18 regression analysis for 25 years. I've been</p> <p>19 qualified as an expert to do regression</p> <p>20 analysis and to do event studies and to</p> <p>21 understand the impact on stock prices of</p> <p>22 particular events.</p> <p>23 So I think that's a short summary</p> <p>24 of my qualifications to do a regression</p> <p>25 analysis and understand the appropriate ways</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 expert in statistics, is that person an expert</p> <p>3 qualified to opine about whether the models</p> <p>4 that were used here were appropriate?</p> <p>5 MR. SOHN: Objection to the extent</p> <p>6 it calls for a legal conclusion.</p> <p>7 A. Again, I'd have to know more about</p> <p>8 your hypothetical. What I would say is if that</p> <p>9 person has expertise in regression and</p> <p>10 statistical analysis, and also has demonstrated</p> <p>11 expertise in event studies and in understanding</p> <p>12 how the stock price moves in response to</p> <p>13 certain events, and has experience in analyzing</p> <p>14 financial markets, financial instruments,</p> <p>15 applying statistical regression principals to</p> <p>16 financial instruments and stock prices, I would</p> <p>17 say he's qualified.</p> <p>18 Q. Okay. What events in terms of</p> <p>19 trading activity affects stock price moves in</p> <p>20 your opinion?</p> <p>21 MR. SOHN: Objection. Is this a</p> <p>22 general question?</p> <p>23 MR. GUIDO: Yes. He just</p> <p>24 testified what he thought was an important</p> <p>25 characteristic.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 to estimate stock price impact of certain</p> <p>3 events.</p> <p>4 Q. Well, I just deposed a scientist</p> <p>5 who does regression analysis in determining the</p> <p>6 effect of the predictiveness of a protein</p> <p>7 called P65 as a predictor of cancer. And he</p> <p>8 knew a lot about statistics and he knew a lot</p> <p>9 about DNA analysis.</p> <p>10 Is he qualified to testify about</p> <p>11 whether or not these models are correct?</p> <p>12 MR. SOHN: Objection. I don't</p> <p>13 know if that's -- if that's asking for a legal</p> <p>14 conclusion.</p> <p>15 BY MR. GUIDO:</p> <p>16 Q. In your view.</p> <p>17 A. I don't know enough -- I don't</p> <p>18 know enough about his background to make that</p> <p>19 decision and.</p> <p>20 Q. Just assume that that's all you</p> <p>21 know.</p> <p>22 MR. SOHN: Objection.</p> <p>23 A. Then I can't -- then I'll -- then</p> <p>24 I'd say I don't know enough.</p> <p>25 Q. Okay. If a person only was an</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 BY MR. GUIDO:</p> <p>3 Q. And I'm just asking what --</p> <p>4 what -- you know, what factors in your view, in</p> <p>5 terms of trading, affect stock price movements.</p> <p>6 A. Well, I think you asked that</p> <p>7 question of me before. And I said there were a</p> <p>8 number of ways a trade as an event can affect a</p> <p>9 stock price. One is through information</p> <p>10 effects; two is through inventory effects on</p> <p>11 broker-dealer stocks. Those are at least two</p> <p>12 channels through which a stock price -- a trade</p> <p>13 can have impacts on a stock price. And I think</p> <p>14 that's generally recognized.</p> <p>15 Q. Well, in this case did you measure</p> <p>16 inventory effect on stock prices?</p> <p>17 A. No, we did not. We measured the</p> <p>18 effect of the trade on the daily stock price</p> <p>19 change, which is a perfectly legitimate way to</p> <p>20 conduct an event study and measure the effect</p> <p>21 of a trade on -- or a number of trades on the</p> <p>22 stock price.</p> <p>23 Q. And you did six regressions, two</p> <p>24 of which you discarded?</p> <p>25 MR. SOHN: Objection.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. We did 18 regressions, none of</p> <p>3 which we discarded, all of which we included</p> <p>4 and considered.</p> <p>5 Q. Let me -- let me shift a little</p> <p>6 bit here and ask you another series of</p> <p>7 questions.</p> <p>8 When I deposed Mr. Beloreshki, I</p> <p>9 found it a little confusing of what his answers</p> <p>10 were. And I'm trying to get a better sense of</p> <p>11 what a regression analysis means to you and to</p> <p>12 him.</p> <p>13 And I guess my first question is:</p> <p>14 What is the hypothesis that is being tested in</p> <p>15 these regressions?</p> <p>16 A. The hypothesis that is being</p> <p>17 tested in this regression --</p> <p>18 Q. That are in your expert report.</p> <p>19 A. In these regressions, as well as</p> <p>20 the hypothesis that's being tested in the</p> <p>21 parametric and the nonparametric statistics --</p> <p>22 Q. No, I'm asking you just about --</p> <p>23 A. Well, they're the same. It's the</p> <p>24 same hypothesis.</p> <p>25 Q. What's the same hypothesis?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 hypothesis, which is that there is no impact.</p> <p>3 Q. Okay. If the coefficient is</p> <p>4 significantly less than 75 percent, can the</p> <p>5 null hypothesis be rejected?</p> <p>6 A. That question makes no sense from</p> <p>7 a statistical point of view.</p> <p>8 Q. Can you say, based on these</p> <p>9 analyses, that the null hypothesis is true?</p> <p>10 A. Statistics, any kind of</p> <p>11 statistics, cannot allow you to say the null is</p> <p>12 true. You cannot -- I'm sorry, let me back up.</p> <p>13 You can either accept the null</p> <p>14 or -- you can either reject the null or fail to</p> <p>15 reject the null hypothesis.</p> <p>16 Q. Okay.</p> <p>17 A. So if you reject the null -- if</p> <p>18 you fail to reject the null hypothesis, that's</p> <p>19 the best you can do.</p> <p>20 Q. Okay.</p> <p>21 A. You can fail to reject the</p> <p>22 hypothesis that there's no impact of Rhino's</p> <p>23 trading activity on the stock price. That's</p> <p>24 the way I set up my tests. That's the way</p> <p>25 Glosten and Jones set up their tests. That's</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. It's the same hypothesis that</p> <p>3 Professors Glosten and Jones used in their</p> <p>4 analysis, which is the null hypothesis is that</p> <p>5 there's no impact.</p> <p>6 Q. So it's fair to say that the</p> <p>7 hypothesis that's being tested is that there's</p> <p>8 no relationship between Badian's activity and</p> <p>9 the Sedona stock price?</p> <p>10 A. The hypothesis that's being tested</p> <p>11 is that there's no impact of the Rhino trades,</p> <p>12 or whatever other measure of the trades is that</p> <p>13 you want to use -- trading activity,</p> <p>14 transactions -- on the stock price. Exactly</p> <p>15 the same as Professors Glosten and Jones' null</p> <p>16 hypothesis, and exactly the same as the null</p> <p>17 hypothesis we used in our nonregression tests.</p> <p>18 Q. Now, is it fair to say that if the</p> <p>19 coefficient significant -- is significant at</p> <p>20 95 percent, the null hypothesis can be</p> <p>21 rejected?</p> <p>22 A. If the coefficient is significant</p> <p>23 at 95 percent, properly measured, with Alpha</p> <p>24 being the threshold "P" value properly</p> <p>25 measured, then you can reject the null</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 the way pretty much everybody in the academic</p> <p>3 literature who's ever done research sets up</p> <p>4 their tests.</p> <p>5 MR. SOHN: Mr. Guido, I don't know</p> <p>6 if now is a good time, but we're --</p> <p>7 MR. GUIDO: What time do you have?</p> <p>8 MR. SCHECHTMAN: Ten to one.</p> <p>9 MR. GUIDO: Ten to one? Okay.</p> <p>10 We'll come back at 1:30?</p> <p>11 MR. SOHN: Okay. You didn't even</p> <p>12 let me say what it's a good time for.</p> <p>13 THE VIDEOGRAPHER: Going off the</p> <p>14 record at 12:52 p.m.</p> <p>15 (A recess is taken.)</p> <p>16</p> <p>17</p> <p>18</p> <p>19</p> <p>20</p> <p>21</p> <p>22</p> <p>23</p> <p>24</p> <p>25</p>

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<p>1 - STEPHEN D. PROWSE - 2 AFTERNOON SESSION 3 THE VIDEOGRAPHER: Going back on 4 the record at 1:38 p.m. 5 BY MR. GUIDO: 6 Q. Mr. Prowse, in -- would you take a 7 look at Exhibit No. 4 again, your report? 8 MR. GUIDO: Preferably if he 9 could have the one that has the color, I 10 would... 11 BY MR. GUIDO: 12 Q. When you were retained to work on 13 that report, did you direct anyone to engage in 14 any statistical or empirical studies? 15 A. Yes, I think I testified earlier 16 that I directed -- after discussions with 17 Mr. Belorshki, I directed Erica Rose to 18 perform statistical and econometric studies, 19 yes. Analysis. 20 Q. Were they included in the text of 21 that report? 22 A. You had me on Exhibit 4. Now 23 you're talking about the text? 24 Q. Just the whole text -- 25 A. Oh, Deposition Exhibit 4?</p>	<p>1 - STEPHEN D. PROWSE - 2 I -- have you been through the disk that -- the 3 information you produced to DLA Piper after you 4 received the subpoena? 5 A. I have not been through that disk. 6 Q. I have. 7 Is there anything in that that you 8 asked Erica to do that is not in that set of 9 materials that you produced to the SEC? 10 MR. SOHN: Objection. 11 A. Well, I haven't looked at the disk 12 you have, so I can't answer that a hundred 13 percent. But all of the analyses, 14 statistical -- all of the analyses, as I 15 understand it, were contained in a set of work 16 sheets that were produced. 17 Q. And they were prepared in 2003 and 18 2004. Isn't that correct? 19 A. I believe some of the old tabs 20 were done before I -- before we were retained 21 on this matter. 22 Q. We -- 23 A. Before we -- 24 Q. Before we, FTI? 25 A. Before we, FTI, were retained on</p>
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<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: The deposition is 3 Exhibit 4. 4 A. The deposition is Exhibit 4. I'm 5 sorry. 6 So, sorry, could you repeat the 7 question? 8 Q. Well, when you were retained, and 9 I think it was November 4th -- 10 A. Yes. 11 Q. -- did you direct anyone to 12 perform any statistical or economic studies at 13 that point in time? 14 A. Yes. 15 Q. Who? 16 A. Erica Rose. 17 Q. Okay. And what studies did you 18 direct her to do? 19 A. I asked her to -- Tsvetan and I 20 agreed on the statistical and regression 21 anal -- analyses and the various tests we 22 wanted to run and the various nonstatistical 23 analyses we wanted done. And we directed her 24 to do all of that, and she did. 25 Q. Now, let me ask you a question:</p>	<p>1 - STEPHEN D. PROWSE - 2 this matter when Mr. Belorshki was at NERA. 3 But regardless of what was done then, we redid 4 or did anew all of the statistical analyses 5 that we thought was required for this report. 6 Q. Well, specifically what 7 statistical analyses was done for the report, 8 Exhibit No. 4, after you were retained? 9 A. The statistical analyses breaks 10 down into three groups: There is the 11 regression analysis, where we asked for 18 12 regressions to be performed, nine in the 13 period -- the entire trading period for Rhino, 14 and the same nine for a smaller period, March 15 1st through May 31st, 2001. 16 Then we ad -- then we directed 17 tests to be run, nonparametric statistical 18 tests and parametric statistical tests to be 19 run. Again, in those two periods; the longer 20 period that encompasses all of Rhino's trading 21 and the shorter period, March 1 through May 31, 22 2001. And those tests were performed. And 23 some, but not all, were actually reported in 24 the report. But my understanding is all of 25 the -- all of that analysis was produced.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, I understand that. But take</p> <p>3 a look at Exhibit 14 again.</p> <p>4 Is there any regression in Exhibit</p> <p>5 No. 14 that wasn't done prior to your retention</p> <p>6 to sign on to Exhibit No. 4?</p> <p>7 A. Is there any regression that</p> <p>8 wasn't done --</p> <p>9 Q. -- prior to you being hired to</p> <p>10 prepare the report, Exhibit No. 4.</p> <p>11 A. Well, I don't know exactly what</p> <p>12 was done prior to me being retained.</p> <p>13 Q. Okay. So, then, you don't know</p> <p>14 whether or not anything was done new after you</p> <p>15 were retained?</p> <p>16 A. I know that everything was done</p> <p>17 new in the sense that the regressions were</p> <p>18 rerun. Even if they had been run -- even if --</p> <p>19 even if the same specification had been run on</p> <p>20 the same time period prior to our engagement,</p> <p>21 prior to FTI's engagement, I know that that</p> <p>22 regression was rerun after we were engaged.</p> <p>23 Q. And --</p> <p>24 A. So -- and the regressions and the</p> <p>25 statistical analysis that were either done anew</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, I'm not sure I understand</p> <p>3 your question. I directed Erica Rose to do</p> <p>4 nine regressions in both periods. She reported</p> <p>5 back to me the results of those nine</p> <p>6 regressions.</p> <p>7 Q. Okay. Now --</p> <p>8 A. In each period.</p> <p>9 Q. Were any of those nine regressions</p> <p>10 different from the nine regressions you were</p> <p>11 told had previously been performed?</p> <p>12 A. I wasn't told anything about what</p> <p>13 was previously performed.</p> <p>14 Q. I thought you told me that</p> <p>15 initially you were told nine regressions were</p> <p>16 performed and you told them to go back and redo</p> <p>17 them?</p> <p>18 A. No, I wasn't told -- no, I didn't</p> <p>19 say that. What I said was --</p> <p>20 Q. Well, the record will show what</p> <p>21 you said.</p> <p>22 A. -- that my understanding is that</p> <p>23 some of the regressions that I asked to be run</p> <p>24 may have been run -- may have been run in a --</p> <p>25 prior to FTI being retained on this matter and</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 or redone, I just described to you.</p> <p>3 Q. Okay. Now, just take Exhibit 14.</p> <p>4 You said there's statistical regression</p> <p>5 analyses for March 1st through May 31. And</p> <p>6 there's a similar sheet for the longer time</p> <p>7 period. Each of these regressions has certain</p> <p>8 variables included in it.</p> <p>9 Did you participate in deciding</p> <p>10 what the variables were to be included in each</p> <p>11 of these regressions you had done?</p> <p>12 A. I participated in deciding that we</p> <p>13 should run nine regressions and that -- and the</p> <p>14 specification of those regressions.</p> <p>15 Q. Okay. Let's take -- did</p> <p>16 someone -- when you made that decision, did</p> <p>17 someone tell you that they had done nine</p> <p>18 regressions and what the specifications were in</p> <p>19 those regressions?</p> <p>20 A. Yes.</p> <p>21 Q. Okay. And --</p> <p>22 A. And what the results were.</p> <p>23 Q. Okay. And did you then tell them</p> <p>24 to go back and redo those specific regressions?</p> <p>25 MR. SOHN: Objection to form.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 over a similar time period.</p> <p>3 Q. In Exhibit 14, okay, is there any</p> <p>4 regression in here that you know had not been</p> <p>5 run prior to being retained?</p> <p>6 A. I'm not sure. I don't believe,</p> <p>7 although I may be wrong, I don't believe that</p> <p>8 the period March 1 through May 31 was looked at</p> <p>9 prior to FTI being retained. I may be wrong on</p> <p>10 that, but that's my belief.</p> <p>11 Q. Okay. But that's a time issue.</p> <p>12 Okay? I'm asking you about --</p> <p>13 A. Right. A time period defines a</p> <p>14 regression.</p> <p>15 Q. Okay. Well, okay, fine. You</p> <p>16 didn't answer.</p> <p>17 But putting the time period aside,</p> <p>18 were any of the models for the regressions, can</p> <p>19 you point to any of those that you directed be</p> <p>20 done after you became part of the team working</p> <p>21 on the report that had not been done prior to</p> <p>22 the time you became a member of the team?</p> <p>23 A. My understanding is that the</p> <p>24 models that Tsvetan -- that Mr. Belorshki and</p> <p>25 I agreed were the appropriate models to be run</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 were similar to the models that had been run</p> <p>3 prior to FTI being retained.</p> <p>4 Q. Do you know, can you tell us how</p> <p>5 they differed in any way?</p> <p>6 A. I can't -- I can't tell you that.</p> <p>7 Q. Can you tell me that they did? Do</p> <p>8 you think --</p> <p>9 A. I can't tell you that they did</p> <p>10 differ.</p> <p>11 Q. Now, the -- you indicated that you</p> <p>12 also asked Erica to do economic analyses that</p> <p>13 were different than the regression analyses</p> <p>14 that are reflected in Exhibit No. 14. Is</p> <p>15 that -- is that correct?</p> <p>16 A. I believe what I said was -- I</p> <p>17 asked for nonregression analysis to be done.</p> <p>18 Q. Can you give us an example of what</p> <p>19 you mean by a nonregression analysis by looking</p> <p>20 at Exhibit No. 4?</p> <p>21 A. For example, all of the analysis</p> <p>22 in Section 3 of the report.</p> <p>23 Q. That's paragraphs 34 through --</p> <p>24 A. Forty-eight.</p> <p>25 Q. Through 50. Right?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 understanding what market manipulation means.</p> <p>3 Do you see the sentence, the last</p> <p>4 sentence says, "In other words, the decline in</p> <p>5 Sedona's stock price was consistent with</p> <p>6 factors that were unrelated to the alleged</p> <p>7 market manipulation by Rhino."</p> <p>8 I used the term "Badian." We'll</p> <p>9 use your term.</p> <p>10 What do you mean by "the alleged</p> <p>11 market manipulation"? What is the alleged</p> <p>12 Market manipulation you're referring to</p> <p>13 there?</p> <p>14 A. I believe the alleged market</p> <p>15 manipulation is referring to the allegations</p> <p>16 that Rhino engaged in market manipulation to</p> <p>17 move the stock price in certain directions.</p> <p>18 Q. And what was the market</p> <p>19 manipulation Rhino was alleged to have engaged</p> <p>20 in based on your understanding of the</p> <p>21 Complaint?</p> <p>22 A. Well, their -- their Complaint's</p> <p>23 not entirely clear as to the period that is</p> <p>24 encompassed by the manipulation. There's a</p> <p>25 variety of different periods that are talked</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Oh, through -- through 50.</p> <p>3 Correct.</p> <p>4 Q. Okay. Now --</p> <p>5 A. And, in addition, there's other</p> <p>6 nonregression analysis.</p> <p>7 Q. Let's just stick with that.</p> <p>8 A. Okay.</p> <p>9 Q. There -- there are other</p> <p>10 nonregression analysis they asked you to do.</p> <p>11 But, first, is this analysis -- the analysis</p> <p>12 that is reflected in 34 through 50. Okay?</p> <p>13 Were any of those analyses,</p> <p>14 analyses that had not been done prior to you</p> <p>15 becoming a part of the team to prepare Exhibit</p> <p>16 No. 4?</p> <p>17 A. I don't know what had been done</p> <p>18 prior and what hadn't.</p> <p>19 Q. Okay. So you don't know whether</p> <p>20 or not any of these were new?</p> <p>21 A. I don't know whether any of these</p> <p>22 were new in the sense that they had not been</p> <p>23 done prior.</p> <p>24 Q. Now, did you direct -- look at</p> <p>25 paragraph 35. I'm back to my problem with</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 about. But I would say it goes from, maybe,</p> <p>3 January '01 through April or May of '01.</p> <p>4 Q. Okay. So that's one. Badian was</p> <p>5 actually -- you use Rhino -- active during that</p> <p>6 period of time.</p> <p>7 And what activity do you</p> <p>8 understand was manipulative during that time</p> <p>9 period, or was alleged to have occurred in that</p> <p>10 time period?</p> <p>11 A. I think it's alleged that Badian</p> <p>12 is alleged to have -- or that Rhino is alleged</p> <p>13 to have traded in a manner to try to drive the</p> <p>14 stock price down and to inject false</p> <p>15 information into the market. I think that's</p> <p>16 the allegations.</p> <p>17 Q. Okay. Now, I read the Complaint.</p> <p>18 I don't see where it says Rhino is the one who</p> <p>19 pushed the price down. I see allegations that</p> <p>20 Badian pushed the price down and Badian said</p> <p>21 certain things at certain times.</p> <p>22 Is the Complaint about Rhino or is</p> <p>23 it about Badian?</p> <p>24 A. I would have to look at the</p> <p>25 Complaint to understand that. My understanding</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 through counsel is that there's maybe a</p> <p>3 complicated relationship with the various</p> <p>4 trades and that we were just to assume that</p> <p>5 Rhino -- we were just to use "Rhino." And I</p> <p>6 think that's what we agreed upon in our initial</p> <p>7 discussion.</p> <p>8 Q. So you agreed that you would use</p> <p>9 the term "Rhino" with counsel for Mr. Badian?</p> <p>10 A. Just at instruction of counsel. I</p> <p>11 don't have an opinion on --</p> <p>12 Q. No, I understand. I'm just --</p> <p>13 A. -- on the actual engagement of the</p> <p>14 trades.</p> <p>15 Q. Okay.</p> <p>16 A. And to the -- to the extent I can</p> <p>17 see the data and I can see who trades, then I</p> <p>18 can see it's, you know, through Pond and Refco,</p> <p>19 but I don't have an opinion as to whether it's</p> <p>20 Badian or Rhino.</p> <p>21 Q. But you were told to use the term</p> <p>22 "Rhino"?</p> <p>23 A. I was -- we were asked to use the</p> <p>24 term "Rhino." That was not part of our task to</p> <p>25 determine --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I'd have to look at the Complaint</p> <p>3 to be specific.</p> <p>4 Q. You're not opining on Badian's</p> <p>5 intent, are you?</p> <p>6 A. No, I'm not -- I'm not opining on</p> <p>7 Badian's intent.</p> <p>8 Q. You're not opining anything on the</p> <p>9 state of mind?</p> <p>10 A. I'm not.</p> <p>11 Q. I mean, so, when you use the term</p> <p>12 "market manipulation," you're really talking</p> <p>13 about affecting price movement.</p> <p>14 Is that a fair characterization?</p> <p>15 A. I think that would be a fair</p> <p>16 characterization.</p> <p>17 Q. Okay.</p> <p>18 A. Affecting price movement.</p> <p>19 Q. And, also, another use of the term</p> <p>20 "market manipulation" is interjecting of false</p> <p>21 information into the marketplace?</p> <p>22 A. I think that's a -- I think that's</p> <p>23 actually a legal requirement based on my lay</p> <p>24 understanding of the law.</p> <p>25 Q. Where'd you -- where'd you get</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Who asked you to use the term</p> <p>3 "Rhino"?</p> <p>4 A. Counsel.</p> <p>5 Q. Which counsel?</p> <p>6 A. I can't remember. Someone at DLA</p> <p>7 Piper.</p> <p>8 Q. Okay. Someone representing</p> <p>9 Badian?</p> <p>10 A. Someone representing Badian,</p> <p>11 correct.</p> <p>12 Q. Now, one of the allegations you</p> <p>13 said is that Badian traded to push the price</p> <p>14 down. Is that alleged in the Complaint? Is</p> <p>15 that your understanding of the Complaint?</p> <p>16 A. I would have to look at the</p> <p>17 Complaint to be more specific, but I think one</p> <p>18 of the allegations is that the trades were</p> <p>19 alleged to have been -- were alleged to have</p> <p>20 pushed the price down, yes.</p> <p>21 Q. Okay. And it was alleged that</p> <p>22 Badian intended to push the price down.</p> <p>23 Is that your understanding?</p> <p>24 A. I can't remember.</p> <p>25 Q. Okay.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 that understanding from of the law? From</p> <p>3 Mr. Sohn?</p> <p>4 A. No.</p> <p>5 Q. From Ms. Schechtman?</p> <p>6 A. No. Just general knowledge.</p> <p>7 Q. Based on your reading ASTI, which</p> <p>8 you asked Ms. Schechtman to send you?</p> <p>9 A. Maybe reading ASTI, yeah.</p> <p>10 Q. What about reading GFL?</p> <p>11 A. I can't remember if I've read -- I</p> <p>12 don't know what you refer to as GFL.</p> <p>13 Q. Well, did you read Ms. Schechtman</p> <p>14 and Mr. Beloreshki's piece before you prepared</p> <p>15 your report?</p> <p>16 A. Yes.</p> <p>17 Q. Okay. Could you have gotten it</p> <p>18 from that?</p> <p>19 A. I don't know. I'd have to look.</p> <p>20 Q. We'll take a look.</p> <p>21 So, one of the questions in this</p> <p>22 that you were addressing is whether or not</p> <p>23 false information was reported to the market?</p> <p>24 A. No, that's what -- you asked what</p> <p>25 I thought was alleged in the Complaint, and I</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 think that is alleged in the Complaint.</p> <p>3 Q. So, when you say that there was no</p> <p>4 market manipulation, are you saying there was</p> <p>5 no false information interjected into the</p> <p>6 marketplace here based on your analysis of the</p> <p>7 Sedona trades by Badian?</p> <p>8 A. I can't say that the -- the</p> <p>9 statistical analysis we do shows no support for</p> <p>10 that allegation.</p> <p>11 Q. I see.</p> <p>12 Did you -- but I thought you said</p> <p>13 the statistical analysis just told you whether</p> <p>14 the price moved or didn't move.</p> <p>15 A. That's correct. And if there's</p> <p>16 false information interjected into the market,</p> <p>17 you would expect the price to move.</p> <p>18 Q. Does the SEC have to show that the</p> <p>19 price moves to bring a 10b case for injecting</p> <p>20 of false information into the market?</p> <p>21 MR. SOHN: Objection. This is a</p> <p>22 totally inappropriate question --</p> <p>23 A. I don't know what -- I don't know</p> <p>24 what the law is. I'm not a lawyer, so I can't</p> <p>25 speak to that.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Emerald account when you reviewed the trade</p> <p>3 data?</p> <p>4 A. Again, wash trades is a term that</p> <p>5 -- I think that's a legal or a tax term. I'm</p> <p>6 not a tax expert. I'm not a legal expert. I</p> <p>7 noticed some trades identified -- maybe alleged</p> <p>8 as wash trades and maybe identified by Glosten</p> <p>9 and Jones in their report as alleged trades.</p> <p>10 So I'm aware of those -- I'm aware</p> <p>11 of those trades, if that's what you're asking.</p> <p>12 Q. Well, what's your -- what's your</p> <p>13 understanding of the term "wash trade"?</p> <p>14 A. I have a very general, lay</p> <p>15 understanding of a wash trade.</p> <p>16 Q. Okay. And what is it?</p> <p>17 A. A trade made by the same person, a</p> <p>18 buy and a sell, in order to reap some tax</p> <p>19 advantage.</p> <p>20 Q. So, in other words, it's a trade</p> <p>21 by me in my account at what used to be Merrill</p> <p>22 with me in my account at Schwab. Is that a</p> <p>23 wash trade?</p> <p>24 MR. SOHN: Objection.</p> <p>25 Q. It's a hypothetical.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, it sounded like that's what</p> <p>3 you were saying. I'm just asking you to</p> <p>4 clarify.</p> <p>5 A. No, what I'm saying is that the</p> <p>6 statistical analyses we do shows no support for</p> <p>7 any -- any notion that Rhino's trades at any</p> <p>8 time influenced the price. One --</p> <p>9 Q. Did you look at --</p> <p>10 A. Can you let me finish, please?</p> <p>11 MR. SOHN: Mr. Guido, he is --</p> <p>12 Q. I'm sorry.</p> <p>13 A. Can you let me finish?</p> <p>14 Q. I'm sorry.</p> <p>15 A. I'm sorry, you'll have to -- could</p> <p>16 you read me back my answer?</p> <p>17 (Whereupon, the record is read</p> <p>18 back.)</p> <p>19 A. Influenced the price. And</p> <p>20 presumably the only way false information --</p> <p>21 false information injected into the market can</p> <p>22 work is if it moves the price.</p> <p>23 Q. Well, let me ask you something:</p> <p>24 Did you -- did you see any wash trades between</p> <p>25 the Westminster Emerald account and the Refco</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, again, I'm not a tax expert</p> <p>3 and I'm not a legal expert. So my</p> <p>4 understanding is either a trade made by -- a</p> <p>5 sell followed by an immediate buy by me,</p> <p>6 regardless of who the parties are, of the same</p> <p>7 stock in order to gain a tax -- tax advantage.</p> <p>8 That's my -- that's my lay</p> <p>9 understanding. I don't have a good legal</p> <p>10 understanding of what a wash trade is. I know</p> <p>11 there are some alleged wash trades in the</p> <p>12 Complaint and I know what they are and I know</p> <p>13 they've been identified.</p> <p>14 Q. Didn't you claim to be an expert</p> <p>15 at the outset of your testimony on financial</p> <p>16 markets?</p> <p>17 A. Financial markets, financial</p> <p>18 instruments, financial risks associated with</p> <p>19 financial instruments. The risks associated</p> <p>20 with small firms raising finance. Yes, all</p> <p>21 that.</p> <p>22 Q. What about an expert in trading</p> <p>23 -- trading in financial instruments? Are</p> <p>24 you an expert in trading in financial</p> <p>25 instruments?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I believe I have the expertise to</p> <p>3 analyze the impact of trading, yes.</p> <p>4 Q. Well --</p> <p>5 A. On the stock price.</p> <p>6 Q. I mean, could one of the things</p> <p>7 that you might be curious about is whether or</p> <p>8 not trades are being reported between the same</p> <p>9 person?</p> <p>10 A. I know what those trades are --</p> <p>11 MR. SOHN: Objection.</p> <p>12 A. -- and they were taken into</p> <p>13 account in our analysis.</p> <p>14 Q. They were?</p> <p>15 A. Yeah.</p> <p>16 Q. Look at -- where do you see the</p> <p>17 Westminster to Refco trades taken into account</p> <p>18 in your expert report?</p> <p>19 A. We took account of all the trades</p> <p>20 made by the accounts in this matter. And</p> <p>21 whether they were -- whether they were normal</p> <p>22 market trades, whether they were what you might</p> <p>23 call wash trades. They're all in our data.</p> <p>24 They're all in our data. So in our analyses</p> <p>25 they are taken into account.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 will -- it will account for the effect -- the</p> <p>3 effect of both of them.</p> <p>4 Q. But it doesn't do a comparative</p> <p>5 analysis of the two?</p> <p>6 MR. SOHN: Objection to form.</p> <p>7 A. It doesn't do a comparative</p> <p>8 analysis, no.</p> <p>9 Q. Thank you.</p> <p>10 Now, you -- you make some</p> <p>11 statements in here about you had Erica do some</p> <p>12 studies about non -- about market and industry</p> <p>13 peer group factors. And one of the questions I</p> <p>14 think I asked you earlier is, had you done any</p> <p>15 regression analyses on the relationship between</p> <p>16 Sedona's stock price movement and the NASDAQ</p> <p>17 price movement? And you indicated you had and</p> <p>18 that for the longer period of time, it showed</p> <p>19 the statistical correlation, and for the</p> <p>20 shorter period of time it did not.</p> <p>21 Now, my question for you is, did</p> <p>22 you do a similar analysis for the peer groups?</p> <p>23 A. By "similar analysis" you mean</p> <p>24 analysis -- a regression analysis involving the</p> <p>25 peer groups?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Did you do a separate analysis of</p> <p>3 the wash trades to see what their impact was in</p> <p>4 the sells?</p> <p>5 A. We didn't do a separate analysis,</p> <p>6 but we did an analysis with them in it.</p> <p>7 Q. Did you do an analysis comparing</p> <p>8 those transactions with other sets of</p> <p>9 transactions?</p> <p>10 MR. SOHN: Objection to the form.</p> <p>11 A. What are those transactions?</p> <p>12 Q. In the -- take, for example, the</p> <p>13 wash trades between April 12th and April 19th,</p> <p>14 2001 between Westminster and Refco and</p> <p>15 compare those to the transactions in October of</p> <p>16 2000.</p> <p>17 MR. SOHN: Objection to the form.</p> <p>18 A. In the sense that they're all in</p> <p>19 the database, yes, we did that.</p> <p>20 Q. But --</p> <p>21 A. We took account of them.</p> <p>22 Q. But the database doesn't compare</p> <p>23 the two, does it?</p> <p>24 A. It includes them in the regression</p> <p>25 analysis and in the statistical analysis, so it</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Uh-huh.</p> <p>3 A. No, we did not.</p> <p>4 Q. Why not?</p> <p>5 A. I can't think of a particular</p> <p>6 reason why we didn't. I just can't think here,</p> <p>7 sitting here right now, what the reason was if</p> <p>8 there was a reason.</p> <p>9 Q. Was the reason because the</p> <p>10 capitalization was different in those</p> <p>11 entities?</p> <p>12 A. No.</p> <p>13 MR. SOHN: Objection to form.</p> <p>14 A. That wouldn't have been the</p> <p>15 different -- that wouldn't have been the</p> <p>16 reason. Capitalization of the NASDAQ is</p> <p>17 different.</p> <p>18 Q. Are there -- were there reasons</p> <p>19 because you couldn't develop a sufficient</p> <p>20 database to do an analysis?</p> <p>21 A. I can't -- sitting here, I can't</p> <p>22 think of the reason why we didn't do that</p> <p>23 specific piece of analysis.</p> <p>24 Q. But you determined that it wasn't</p> <p>25 going to be done?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. For a reason I can't remember.</p> <p>3 Q. But you did, for a reason, decide</p> <p>4 not to do it?</p> <p>5 MR. SOHN: Objection.</p> <p>6 A. For some reason.</p> <p>7 Q. Was it a good reason or a bad</p> <p>8 reason?</p> <p>9 MR. SOHN: Objection.</p> <p>10 A. Sitting here, I can't remember</p> <p>11 what the reason was.</p> <p>12 Q. It was just a reason.</p> <p>13 A. I can't remember what the reason</p> <p>14 was.</p> <p>15 Q. But you did discuss it with</p> <p>16 Ms. Beloreshki?</p> <p>17 A. Well, I can't remember -- I can't</p> <p>18 remember --</p> <p>19 Q. Mr. Beloreshki, excuse me.</p> <p>20 A. I can't remember discussing it</p> <p>21 with Mr. Beloreshki. If I did remember</p> <p>22 discussing it, I probably would have remembered</p> <p>23 more of the context around the discussion.</p> <p>24 Q. But you just didn't do it?</p> <p>25 A. I just -- it's not here.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, did you do an event study on</p> <p>3 the issuance of 10-Ks?</p> <p>4 A. We did not do an event study on</p> <p>5 the issuance of 10-Ks. There wouldn't be a</p> <p>6 reason to.</p> <p>7 Q. Did you do any event studies on</p> <p>8 the company's issuance of equity securities?</p> <p>9 A. We did not do an event study on</p> <p>10 the company's issuance of equity securities.</p> <p>11 Q. Did you do an event study on</p> <p>12 any -- any news releases from the company?</p> <p>13 A. Actually, I want to qualify that</p> <p>14 last statement. To the extent that the equity</p> <p>15 issuances were issuances of stock to Rhino, we</p> <p>16 covered that in our database. So we looked at</p> <p>17 that.</p> <p>18 And, also, to the extent your</p> <p>19 question covers issuance of stock due to</p> <p>20 conversions, we looked at that, as well. So I</p> <p>21 just want to qualify that last answer.</p> <p>22 And then, with regards to question</p> <p>23 about news events, we did not do a study, an</p> <p>24 event study, regarding news events.</p> <p>25 Q. I understand your answer, and I</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. It's not here. Okay.</p> <p>3 Now -- then you talk about the</p> <p>4 company-specific factors starting on page 9.</p> <p>5 And I think I had asked you whether you did any</p> <p>6 regression analysis to determine whether or not</p> <p>7 any of the events that you talked about had an</p> <p>8 impact on the -- on the stock price. In the</p> <p>9 event study, excuse me, that had an impact on</p> <p>10 the price. And you indicated you had not done</p> <p>11 that.</p> <p>12 A. No, that's not correct. You were</p> <p>13 talking about Exhibit 8. And you had asked me,</p> <p>14 Did you do an event study around the FPS</p> <p>15 issuance?</p> <p>16 Q. Okay.</p> <p>17 A. The serial FPS issuance that</p> <p>18 Sedona went through throughout its life. And I</p> <p>19 said, no, we didn't do an event study there.</p> <p>20 That wasn't the point of this chart.</p> <p>21 Q. Okay.</p> <p>22 A. We did do event studies, and</p> <p>23 that's what the regression results are. They</p> <p>24 are event studies looking at the impact of</p> <p>25 the -- of the Rhino trading.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 think I understood the reason for your answer</p> <p>3 to my question. But my question -- my</p> <p>4 question, I think, hasn't been answered.</p> <p>5 And my question is, did you do a</p> <p>6 specific event study on the issuance -- around</p> <p>7 the issuance of securities by Sedona?</p> <p>8 MR. SOHN: Asked and answered.</p> <p>9 A. Yes, to the extent that -- to the</p> <p>10 extent that that covers Rhino's purchase of</p> <p>11 shares from Sedona and the conversions.</p> <p>12 Q. Well, is your answer yes, because</p> <p>13 you included it in the regression analyses that</p> <p>14 are in Exhibit No. 4?</p> <p>15 A. The regression analysis and the</p> <p>16 nonregression analysis.</p> <p>17 Q. What's the --</p> <p>18 A. The statistical -- the parametric</p> <p>19 and nonparametric analysis, I believe. I</p> <p>20 believe that includes that, too. I'm not</p> <p>21 sure.</p> <p>22 Q. Show me in Exhibit No. 4.</p> <p>23 A. Well, I believe that some of the</p> <p>24 parametric tests we ran -- I would have to go</p> <p>25 back and check, but I believe some of the</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 parametric tests we ran cover conversions and</p> <p>3 direct issuance of stock. I don't think any of</p> <p>4 the ones reported in the -- in the exhibits to</p> <p>5 Deposition Exhibit 4 do that, but I think some</p> <p>6 of the other parametric or nonparametric tests</p> <p>7 may do that.</p> <p>8 Q. But you can't point to anything in</p> <p>9 this report, an event study on each of those</p> <p>10 specific events?</p> <p>11 A. Well, this -- this wouldn't be an</p> <p>12 event study. This would be a statistical</p> <p>13 analysis of what happens to the stock price on</p> <p>14 days when Rhino buys stock from Sedona. It</p> <p>15 would be an analysis similar in concept to the</p> <p>16 analyses in Exhibits 10 and 11, but it would</p> <p>17 cover -- it would cover direct purchases or</p> <p>18 conversions.</p> <p>19 So I'm not entirely sure, but I</p> <p>20 think -- I think we may have done that in some</p> <p>21 of the other non -- nonregression tests.</p> <p>22 Q. But it's not included in this</p> <p>23 expert report, is it?</p> <p>24 A. There's not an exhibit that</p> <p>25 reports the results of those non --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. And in Regression 3 in your</p> <p>3 report, as I review the report, Regression</p> <p>4 Number 3 talks about various files --</p> <p>5 A. Right.</p> <p>6 Q. -- which were included in the</p> <p>7 data, but there's no stand-alone regression</p> <p>8 analysis for each of the stock issuances in an</p> <p>9 event study to determine what that particular</p> <p>10 event impact was on the price of Sedona stock,</p> <p>11 was there?</p> <p>12 A. There absolutely is, and that's</p> <p>13 the coefficient under the Rhino principal in</p> <p>14 Regression 3. That looks at the events of</p> <p>15 Rhino buying principal. And that principal</p> <p>16 includes two things: One, conversions; two,</p> <p>17 direct purchases.</p> <p>18 Q. What column is that?</p> <p>19 A. Well, it depends how you count the</p> <p>20 columns, but it's the column entitled "Rhino</p> <p>21 principal" in quotation marks in Exhibit 13A</p> <p>22 and 13B.</p> <p>23 Q. I'm sorry, I'm asking you to look</p> <p>24 at Exhibit 14. Tell me where.</p> <p>25 A. Okay. So this may take a while.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 nonregression statistical tests.</p> <p>3 Q. Oh, okay.</p> <p>4 Do you know what the percentage of</p> <p>5 significance was in those regression event</p> <p>6 studies?</p> <p>7 MR. SOHN: Objection to form.</p> <p>8 A. Well, there's -- there's a</p> <p>9 different "P" value for every regression, every</p> <p>10 coefficient. So if you're asking me to recite</p> <p>11 to you all the "P" values, I would have to go</p> <p>12 and look at them to do that. So I'm not sure</p> <p>13 what you're asking.</p> <p>14 Q. Well, were there any "P" values</p> <p>15 that were calculated for each of those events?</p> <p>16 MR. SOHN: Objection to form.</p> <p>17 A. Each of what events?</p> <p>18 Q. The issuance of stock.</p> <p>19 A. As a -- yes, there was, I believe.</p> <p>20 Q. Is that in the documents that you</p> <p>21 pulled together on that disk that you provided</p> <p>22 to counsel after you received the subpoena in</p> <p>23 this case?</p> <p>24 A. No, it's in the results of</p> <p>25 Regression 3 in the report.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. I'll make it easy for you. Look</p> <p>3 at AQ.</p> <p>4 A. AQ. Okay. So AQ looks to be</p> <p>5 Regression 3. AQ.</p> <p>6 Q. It's a subcategory of Regression</p> <p>7 3, isn't it?</p> <p>8 MR. SOHN: Objection to form.</p> <p>9 Q. I think that's referred to as a</p> <p>10 leading question, Mr. Prowse.</p> <p>11 A. Sorry, I was trying to find the --</p> <p>12 find the right Regression 3 here. I'm trying</p> <p>13 to match it up with -- oh, I'm probably looking</p> <p>14 at the wrong exhibit here.</p> <p>15 Q. You're look -- I mean, I've asked</p> <p>16 you to look at Exhibit 14.</p> <p>17 A. I am. I am.</p> <p>18 Q. And I suggested you take a look at</p> <p>19 Column AQ.</p> <p>20 A. Yes, that's correct. That's</p> <p>21 the -- that's the coefficient that is reported</p> <p>22 in Exhibit 13B.</p> <p>23 Q. Okay.</p> <p>24 A. And that matches to Column AQ.</p> <p>25 Q. Okay. Now, the principal in AQ,</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 okay, does that show that there's a</p> <p>3 statistically significant correlation between</p> <p>4 the issuance of stock and Sedona stock</p> <p>5 prices?</p> <p>6 A. It shows that there's not a</p> <p>7 statistically significant relationship between</p> <p>8 issuance of stock as I have defined it and</p> <p>9 Sedona stock price.</p> <p>10 Q. Okay.</p> <p>11 MR. GUIDO: And why don't we take</p> <p>12 a break. I think that the videographer needs</p> <p>13 to change a tape.</p> <p>14 THE VIDEOGRAPHER: This concludes</p> <p>15 Tape Number 2 in the videotaped deposition of</p> <p>16 Mr. Stephen Prowse. Going off the record at</p> <p>17 2:16 p.m.</p> <p>18 (A recess is taken.)</p> <p>19 THE VIDEOGRAPHER: This begins</p> <p>20 Tape Number 3 in the videotaped deposition of</p> <p>21 Dr. Stephen Prowse. Going back on the record</p> <p>22 at 2:24 p.m.</p> <p>23 BY MR. GUIDO:</p> <p>24 Q. The -- take a look at Exhibit No.</p> <p>25 12, that Pet Quarters rebuttal report.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Correct.</p> <p>3 Q. Okay. Would it be fair to</p> <p>4 criticize your report for making allegations</p> <p>5 about Sedona's stock price performance and its</p> <p>6 financial condition and its issuance of</p> <p>7 convertible debentures and the performance of</p> <p>8 its peers in NASDAQ without doing a regression</p> <p>9 analysis?</p> <p>10 MR. SOHN: Objection; compound.</p> <p>11 A. No, it wouldn't.</p> <p>12 Q. Why not?</p> <p>13 A. Well, in part because we do do a</p> <p>14 regression analysis that takes into account</p> <p>15 some of the variables you mentioned: NASDAQ,</p> <p>16 issuance of stock and, the most important</p> <p>17 variable, trades or transactions by Rhino.</p> <p>18 The discussion that we have in</p> <p>19 Section 3 of our report regarding other factors</p> <p>20 that influenced Sedona's stock is meant to be</p> <p>21 illustrative as opposed to, you know,</p> <p>22 quantitative.</p> <p>23 Q. Oh, okay. So you didn't attempt</p> <p>24 to quantify, and you don't believe you had a</p> <p>25 responsibility to do that, even though you said</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 The -- do you recall preparing the</p> <p>3 rebuttal report in Pet Quarters?</p> <p>4 A. Yes.</p> <p>5 Q. And do you recall that one of your</p> <p>6 criticisms of the -- I -- you referred to it as</p> <p>7 the Shapiro/Pham report, is that they had</p> <p>8 failed to do regression analyses to support</p> <p>9 their claims that certain events had an impact</p> <p>10 on the market, or the price of Pet Quarters'</p> <p>11 stock.</p> <p>12 Do you recall that?</p> <p>13 A. If you can direct me to where in</p> <p>14 my report I say that, it would be helpful.</p> <p>15 Q. Well take -- it's very easy. Take</p> <p>16 a look at paragraph 7 of your report.</p> <p>17 A. Yes.</p> <p>18 Q. You see where you point out that</p> <p>19 there's a need to do an event study if you</p> <p>20 argue that any particular event had an impact</p> <p>21 on -- on stock price?</p> <p>22 A. Yes, I see that.</p> <p>23 Q. And you criticize them for</p> <p>24 Shapiro -- the Shapiro/Pham report for not</p> <p>25 doing so?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 that Shapiro Pham had a responsibility to do</p> <p>3 that?</p> <p>4 MR. SOHN: Objection.</p> <p>5 A. Well, Shapiro/Pham -- I can't</p> <p>6 remember exactly what Shapiro/Pham were doing,</p> <p>7 but they didn't -- I think they were alleging</p> <p>8 to estimate the response of a stock price to a</p> <p>9 particular announcement.</p> <p>10 Q. Well --</p> <p>11 A. We are -- I'm not finished.</p> <p>12 Q. Excuse me.</p> <p>13 A. We are in the context of doing an</p> <p>14 event study. We do an event study with regards</p> <p>15 to Rhino's trades in the context of pointing</p> <p>16 out reasons why Sedona's stock price can be</p> <p>17 expected to be, A, highly volatile, and, B, to</p> <p>18 fall.</p> <p>19 We are -- we are performing sort of</p> <p>20 illustrative examples of the types of things</p> <p>21 that would cause the stock price to be volatile</p> <p>22 and to -- and to fall.</p> <p>23 Q. You used illustrative examples</p> <p>24 without doing a regression analysis of those</p> <p>25 illustrative examples. And --</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. We did -- we did do a regression</p> <p>3 analysis of some of the variables you</p> <p>4 mentioned.</p> <p>5 Q. In NASDAQ?</p> <p>6 A. And issuance of stock.</p> <p>7 Q. And you found that there was no</p> <p>8 statistically significant relationship between</p> <p>9 those two, between --</p> <p>10 A. Between Rhino -- between issuance</p> <p>11 of stock to Rhino and stock price.</p> <p>12 Q. Now, the -- the other thing I</p> <p>13 found of interest in your rebuttal report was</p> <p>14 your critique of the Shapiro/Pham report's</p> <p>15 reliance on the certain kinds of trades. And</p> <p>16 if you look at paragraph 48, I think is where</p> <p>17 you address that.</p> <p>18 I think that in this section</p> <p>19 you're addressing the question of what are</p> <p>20 known as wash trades; and that is trades</p> <p>21 between accounts in which the same person is</p> <p>22 the beneficiary of it.</p> <p>23 Is that a fair characterization of</p> <p>24 what you're addressing in these paragraphs 48</p> <p>25 through 52?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Yeah.</p> <p>3 A. I can't remember.</p> <p>4 Q. You don't remember?</p> <p>5 A. I'd have to review this report in</p> <p>6 detail and review the data. So, just reading</p> <p>7 this, I can't tell. But I do believe we're</p> <p>8 looking at trades between accounts and we are</p> <p>9 criticizing their analysis.</p> <p>10 Q. Okay. Well, I mean, paragraph 48</p> <p>11 says that you're addressing the question of</p> <p>12 transactions between the respondents' own</p> <p>13 accounts?</p> <p>14 A. Yes.</p> <p>15 Q. And wasn't that a part of the</p> <p>16 trading with itself?</p> <p>17 MR. SOHN: Objection to form.</p> <p>18 A. I'm not sure I necessarily agree</p> <p>19 with it. I used the language that I've used</p> <p>20 here. What's --</p> <p>21 Q. What's -- what's a respondent?</p> <p>22 A. The respondent in this matter is</p> <p>23 the defendants.</p> <p>24 Q. Okay. And the paragraph is</p> <p>25 addressing those defendants trading with</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 MR. SOHN: Objection to form.</p> <p>3 A. Forty-eight through 53? Did you</p> <p>4 say 48 through 53?</p> <p>5 Q. Well, okay, 53. I mean, I think</p> <p>6 it stopped -- for our purposes it stops at</p> <p>7 paragraph 52. I think 53 addresses a different</p> <p>8 issue.</p> <p>9 A. Well, I don't see the term "wash</p> <p>10 trades" anywhere in this section, so I'm not</p> <p>11 sure what you mean by that.</p> <p>12 Q. Well, it talks about trading</p> <p>13 between matched buyers. Right?</p> <p>14 A. It talks about respondents' trades</p> <p>15 between accounts.</p> <p>16 Q. Okay. And are those between --</p> <p>17 were the facts in those cases the accounts were</p> <p>18 owned by the same party?</p> <p>19 A. I -- I can't recall. It's been a</p> <p>20 long time since I reviewed this report.</p> <p>21 Q. Weren't those transactions between</p> <p>22 Westminster and Refco Emerald accounts?</p> <p>23 MR. SOHN: Objection to form.</p> <p>24 A. Are you talking about the Pet</p> <p>25 Quarters report?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 themselves in two different accounts?</p> <p>3 A. Transactions between defendants'</p> <p>4 own accounts. Correct.</p> <p>5 Q. Okay. And that you conclude that</p> <p>6 the Shapiro/Pham report improperly concluded</p> <p>7 that those transactions interjected false</p> <p>8 information into the market that resulted in a</p> <p>9 price decline.</p> <p>10 Isn't that what you concluded?</p> <p>11 A. We criticized their analysis.</p> <p>12 Q. Okay. And what was the critique</p> <p>13 of their analysis that you made?</p> <p>14 A. Well, it's detailed in paragraphs</p> <p>15 50 through 52 or maybe 53.</p> <p>16 Q. Okay. Well, was one of your</p> <p>17 criticisms that the transactions were</p> <p>18 transactions that were executed at or near the</p> <p>19 ask price as opposed to the bid price? And,</p> <p>20 so, therefore the information interjected in</p> <p>21 the market tended to be positive for the price</p> <p>22 of Pet Quarters' stock?</p> <p>23 MR. SOHN: Objection to the form.</p> <p>24 A. I think we say the only way that</p> <p>25 they, the trades, might inject negative</p>

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<p>1 - STEPHEN D. PROWSE - 2 information into the market would be if they 3 were executed at prices below the bid at the 4 time of the trade. 5 Q. Okay. Take a look at -- 6 A. So if their -- 7 Q. Take a look at the very last page 8 of Exhibit No. 12. 9 A. Is that Exhibit 2? 10 Q. Yes. What is Exhibit 2? 11 A. Exhibit 2 is an exhibit which 12 shows some analysis regarding paragraph 52. 13 Q. Okay. And are these intra-day 14 transactions? 15 A. Intra-day transactions? 16 Q. Yeah. I mean, is this evaluating 17 intra-day data? 18 A. This is evaluating trades. 19 Q. In relationship to what? 20 A. To a bid-ask spread. 21 Q. The bid-ask spread when during the 22 day? 23 A. I believe at the same time the 24 trade was made. I would have to -- 25 Q. So this was --</p>	<p>1 - STEPHEN D. PROWSE - 2 that if there was an intent by respondents in 3 this matter, the Pet Quarters matter, to inject 4 false information into the market, the 5 Shapiro/Pham report fails to offer an 6 explanation for why all inter-account -- 7 inter-account transactions were not in the form 8 of sales. 9 If that was the intent, to inject 10 false information into the market, then why 11 aren't they all in the form of sales as opposed 12 to nonmarket transfers? 13 Q. So, I think what -- I'm a little 14 puzzled by what you just said and let me -- let 15 me ask you a few questions. 16 Now, what you're saying is, is 17 that there couldn't have been false information 18 interjected into the market by nonmarket 19 transfers? 20 A. What I'm saying is if there was an 21 intent to inject false information into the 22 market, there's a failure to explain why all 23 the accounts were not in the form of sales. 24 Because that would seem to be the easiest way 25 to transmit information.</p>
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<p>1 - STEPHEN D. PROWSE - 2 A. I would have to confirm that. 3 Q. Okay. But it's your understanding 4 that that's what this does? 5 A. That's my belief. 6 Q. So is this an analysis of 7 intra-day trading? 8 A. This is an analysis of trades made 9 with the -- with the bid-ask spread. 10 Q. Okay. At -- at or near the time 11 of the bid-ask spread? 12 A. At or -- 13 MR. SOHN: Objection to the form. 14 A. At or near the time of trade. 15 Q. Now, paragraph 53 seems to be 16 talking about the Shapiro/Pham report's failure 17 to exclude nonmarket transfers from its 18 analysis. Is that a fair -- 19 A. No, it's not fair. 20 Q. -- inference to be drawn from that 21 paragraph? 22 A. No. 23 Q. So, why was it important to say 24 that there were three nonmarket transfers? 25 A. I think the intent here was to say</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. Into the market. 3 A. Into the market. 4 Q. Okay. And that would be important 5 to know how the nonmarket trans -- transfers 6 interjected false information into the market? 7 A. It would be important to know if 8 the market -- if the market transactions had an 9 effect on the stock price. 10 Q. And it would be important to 11 factor out the nonmarket transactions to 12 determine whether or not the market 13 transactions did have an impact? 14 A. That would be one way to do it. 15 And that's the way we do it, in fact, in our 16 analysis in the Sedona matter. 17 Q. Well, which regressions that you 18 did that are included in your report exclude 19 nonmarket transactions? 20 A. So, I'm going to need to get my 21 report. 22 MR. SOHN: Here. 23 A. So, if you turn to Exhibit 13 -- 24 and you asked specifically about regressions 25 that excluded nonmarket transactions.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Correct?</p> <p>3 Q. That's correct. That's correct.</p> <p>4 A. Okay. So that would be Regression</p> <p>5 1, Regression 2, Regression 3 and Regression 4.</p> <p>6 They all either exclude them or separate them</p> <p>7 out.</p> <p>8 Q. No, but the regression -- take a</p> <p>9 look at -- take a look at Exhibit No. 14, which</p> <p>10 is the backup for this, and tell me which one</p> <p>11 of those columns of the regressions exclude</p> <p>12 nonmarket transactions.</p> <p>13 A. Well, we discussed this at length</p> <p>14 in the morning. And I'm not sure what you mean</p> <p>15 by "columns," but --</p> <p>16 Q. Well, I mean at the top it has the</p> <p>17 letters at the top. That's what I mean by</p> <p>18 columns.</p> <p>19 Which one of your regressions</p> <p>20 exclude nonmarket transactions?</p> <p>21 A. Well, the regressions in this</p> <p>22 Exhibit 14 that match up with Regression 1,</p> <p>23 Regression 2, Regression 3 and Regression 4 in</p> <p>24 Exhibit 13A or Exhibit 13B are the ones which</p> <p>25 either exclude nonmarket transactions or</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 at spreadsheet 4.</p> <p>3 MR. SOHN: I'm sorry, what are we</p> <p>4 looking at?</p> <p>5 MR. GUIDO: Exhibit No. 14.</p> <p>6 Excuse me.</p> <p>7 BY MR. GUIDO:</p> <p>8 Q. And look at the Columns AS through</p> <p>9 AW, just to clarify the record.</p> <p>10 A. Okay.</p> <p>11 Q. They're dealing with Regression 4</p> <p>12 and an alternative to Regression 4, or 4A.</p> <p>13 Do you see that?</p> <p>14 A. Yes.</p> <p>15 Q. Okay. Regression No. 4, which the</p> <p>16 results are in Column A -- Column AT, are the</p> <p>17 "Net daily shares transactions as percentage of</p> <p>18 volume." And then AW says "Net trading as a</p> <p>19 percentage of volume."</p> <p>20 A. Right.</p> <p>21 Q. In 4A.</p> <p>22 So is it Column AW that's being</p> <p>23 reported on the spreadsheet?</p> <p>24 A. Yes.</p> <p>25 Q. Okay.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 separate them out separately from market</p> <p>3 transactions.</p> <p>4 Q. Okay. Which ones exclude? Forget</p> <p>5 the separate out.</p> <p>6 A. The ones that exclude nonmarket</p> <p>7 transactions are Regressions 1, 2 and 4.</p> <p>8 Q. Look at Exhibit No. 15.</p> <p>9 MR. SOHN: Fifteen?</p> <p>10 MR. GUIDO: Fifteen. Deposition</p> <p>11 Exhibit No. 15.</p> <p>12 Q. And also look at Deposition</p> <p>13 Exhibit Number --</p> <p>14 MR. GUIDO: Can I get back the two</p> <p>15 most recent exhibits?</p> <p>16 MR. SOHN: Twenty-four and --</p> <p>17 MR. GUIDO: Those.</p> <p>18 MR. SOHN: Here are the most</p> <p>19 recent ones.</p> <p>20 BY MR. GUIDO:</p> <p>21 Q. So it's one, two and four that</p> <p>22 exclude the impact of nonmarket transactions?</p> <p>23 A. They exclude nonmarket</p> <p>24 transactions.</p> <p>25 Q. Okay. The reason -- take a look</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. It's being reported in Exhibit</p> <p>3 13B.</p> <p>4 Q. Okay. Thank you.</p> <p>5 Now, so, the Regression 1,</p> <p>6 Regression 2 and Regression 4 do not include in</p> <p>7 any way nonmarket transactions?</p> <p>8 A. Yes, that's my understanding.</p> <p>9 Q. All right. So we've got three</p> <p>10 regressions. And let's take Regression 1. It</p> <p>11 says "Any transaction flag." Okay? Do you see</p> <p>12 that in Column AD, or on Exhibit 13B of your</p> <p>13 expert report, it's the third column. It's</p> <p>14 called "Any Rhino Trading."</p> <p>15 A. Okay. So I'm looking at Column</p> <p>16 AD?</p> <p>17 Q. AD?</p> <p>18 A. Yeah.</p> <p>19 Q. In Exhibit 14.</p> <p>20 A. Yeah.</p> <p>21 Q. It says "Any Transaction Flag."</p> <p>22 And that conforms with "Any Rhino Trading"</p> <p>23 column on Exhibit 13B. Right?</p> <p>24 A. No, it doesn't.</p> <p>25 Q. It does not.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. No.</p> <p>3 Q. Okay. What information in Exhibit</p> <p>4 14 -- what column corresponds to "Any Rhino</p> <p>5 Trading"?</p> <p>6 A. The column in Exhibit 14 that</p> <p>7 corresponds to Regression 1 reported in Exhibit</p> <p>8 13B is Column AF and AG.</p> <p>9 Q. AF and AG?</p> <p>10 A. Yes.</p> <p>11 Q. Okay. All right. So it's a buy</p> <p>12 or sell flag?</p> <p>13 A. Yes.</p> <p>14 Q. Okay. And that is AF and AG.</p> <p>15 Now, with regard to Regression</p> <p>16 Number 2, how does that differ from any Rhino</p> <p>17 trading?</p> <p>18 A. It separates -- separates out the</p> <p>19 effect of Rhino buys from Rhino sells and lets</p> <p>20 them have inde -- independent effects on the</p> <p>21 price of Sedona to investigate whether</p> <p>22 specifically Rhino purchases as opposed to</p> <p>23 Rhino sells, or vice versa, have any impact on</p> <p>24 the price.</p> <p>25 Q. So, in other words, you do two</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 on which there was a buy and a sell.</p> <p>3 Q. Right.</p> <p>4 A. So it's appropriate to capture</p> <p>5 that in both dummies, the buy dummy and the</p> <p>6 sell dummy.</p> <p>7 Q. Okay. And -- and -- and how do</p> <p>8 you use buy dummies as opposed to how do you</p> <p>9 use sell dummies in your regression?</p> <p>10 A. Well, I use them the same. I</p> <p>11 mean, there's a buy dummy -- there's a buy</p> <p>12 dummy variable and there's a sell dummy</p> <p>13 variable. They are treated identically.</p> <p>14 Identically. They're independent variables in</p> <p>15 the regression.</p> <p>16 They're just -- they just have</p> <p>17 different values on different days except</p> <p>18 when -- except on days when Rhino doesn't do</p> <p>19 anything, in which case they're both zeroes.</p> <p>20 And on days when Rhino sells and buys on the</p> <p>21 same day, in which case they're both one. But</p> <p>22 that's --</p> <p>23 Q. Well --</p> <p>24 A. That's no big deal.</p> <p>25 Q. -- in this regression are you</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 separate regressions and then you combine them?</p> <p>3 Is that --</p> <p>4 A. No.</p> <p>5 Q. No? How do you do that</p> <p>6 mathematically?</p> <p>7 A. You just have a dummy variable</p> <p>8 that is zero when Rhino does anything but buy,</p> <p>9 and a one when Rhino buys. That's a dummy or a</p> <p>10 buy flag.</p> <p>11 Q. Okay.</p> <p>12 A. Then you have a dummy that is zero</p> <p>13 for any other -- any time other than -- any day</p> <p>14 other than when Rhino sells, and one if Rhino</p> <p>15 sells. And you just stick them in the same</p> <p>16 regression.</p> <p>17 Q. Well, take a look at line 645,</p> <p>18 6/20/2000, and run it over to AJ and AK, where</p> <p>19 it has these "dummies." And there are two</p> <p>20 ones.</p> <p>21 A. Correct.</p> <p>22 Q. How do you distinguish between the</p> <p>23 two ones and those that have just a one in one</p> <p>24 of the columns?</p> <p>25 A. Well, that was a day, obviously,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 comparing buy days against sell days?</p> <p>3 A. Where -- in this regression, which</p> <p>4 is Regression 2, we are looking -- Regression 2</p> <p>5 in Exhibit 13B. We are looking at whether</p> <p>6 there is an indi -- an effect specific to Rhino</p> <p>7 buys on Sedona stock price, and simultaneously</p> <p>8 we are looking at whether there is an effect</p> <p>9 specific to Rhino sells on Sedona stock price.</p> <p>10 Q. So this is not comparing the</p> <p>11 results on days where there's a sell flag with</p> <p>12 the days where there are buy flags? This</p> <p>13 Regression Number 2.</p> <p>14 A. I don't know what you mean by</p> <p>15 that. You can -- you could compare the</p> <p>16 coefficients of the Rhino buy dummy with the</p> <p>17 Rhino sell dummy if you wanted to, if that's</p> <p>18 what you mean.</p> <p>19 Q. Can I use any of these numbers</p> <p>20 that you've -- that you've come up with under</p> <p>21 AJ and AK to figure out what that relationship</p> <p>22 would be?</p> <p>23 MR. SOHN: Objection to the form.</p> <p>24 A. Relationship between what?</p> <p>25 Q. Between comparing sell days and</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 buy days.</p> <p>3 A. Well, you can either do that by</p> <p>4 looking at Column AJ or AK, or you can do that</p> <p>5 by looking at the two columns in Exhibit 13B</p> <p>6 underneath Rhino purchases and Rhino sales.</p> <p>7 One will be .01 point estimate of</p> <p>8 the coefficient, and one will be a negative .04</p> <p>9 point coefficient grounded. It's actually</p> <p>10 .036, but -- negative .036.</p> <p>11 Q. Okay. So taking these days, okay,</p> <p>12 what you're doing is that you're designating a</p> <p>13 day as a day when Badian was trading as opposed</p> <p>14 to days he was not?</p> <p>15 A. That is what regression -- that is</p> <p>16 not what Regression 2 does. That's --</p> <p>17 Regression 1 looks at the difference between</p> <p>18 when Rhino was trading and when Rhino was not</p> <p>19 trading.</p> <p>20 Q. Okay.</p> <p>21 A. Regression 2 looks at the</p> <p>22 difference between Rhino when -- between --</p> <p>23 looks at the effect of when Rhino was selling</p> <p>24 and then, separately, the effect of when Rhino</p> <p>25 was buying.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 trades.</p> <p>3 Q. Well, suppose that on one of those</p> <p>4 days where you put a one is that Badian's</p> <p>5 activity pushes the Sedona -- or as a result --</p> <p>6 or occurs at the time. Excuse me. The</p> <p>7 causation, rather.</p> <p>8 Suppose that on a day Badian's</p> <p>9 activity -- Badian trades, and the price goes</p> <p>10 down 5 percent and he had -- his activity</p> <p>11 involved the selling of five thousand shares.</p> <p>12 And on another day you have a one, and that he</p> <p>13 trades/sells five hundred shares and the price</p> <p>14 goes down 1 percent.</p> <p>15 Does this regression formula take</p> <p>16 into consideration the impact of the size of</p> <p>17 his sales?</p> <p>18 MR. SOHN: Objection to the form.</p> <p>19 A. The regression does not take into</p> <p>20 account the impact of the size of the trade.</p> <p>21 It takes into account whether there was a trade</p> <p>22 or not.</p> <p>23 Q. When you -- are you aware that the</p> <p>24 literature that addresses the question of the</p> <p>25 impact of trading on market price indicates</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Okay. Let's go back to -- let's</p> <p>3 focus on Regression 1 now.</p> <p>4 I gather the variable any day of</p> <p>5 trading indicates by a one the days that Rhino</p> <p>6 or Badian traded Sedona stock. Is that</p> <p>7 correct?</p> <p>8 A. The days when Rhino had a -- had a</p> <p>9 trade, right.</p> <p>10 Q. Okay.</p> <p>11 A. Whether it was a buy or whether it</p> <p>12 was a sell.</p> <p>13 Q. Okay. And do the results indicate</p> <p>14 the coefficient that measures the difference in</p> <p>15 the average daily Sedona returns on the days</p> <p>16 that Rhino traded compared to days that Rhino</p> <p>17 did not trade?</p> <p>18 A. Could you repeat that question or</p> <p>19 read it back?</p> <p>20 MR. GUIDO: Would you read that</p> <p>21 back, please?</p> <p>22 (Whereupon, the record is read</p> <p>23 back.)</p> <p>24 A. The coefficient measures the</p> <p>25 effect on Sedona's stock returns when Rhino</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 that the quantity, the size, of the sell or buy</p> <p>3 activity should be included in the measurement</p> <p>4 to determine a significant relationship between</p> <p>5 price and trading?</p> <p>6 MR. SOHN: Objection to the form.</p> <p>7 A. I'm generally aware that there are</p> <p>8 some results that suggest that's a measure of</p> <p>9 trading that could be used to measure the</p> <p>10 impact of a trade, the size of it, or the size</p> <p>11 of it relative to volume. But I'm also aware</p> <p>12 of numerous results that look at just whether</p> <p>13 there was a trade or not.</p> <p>14 Q. Well, I'm asking -- I mean, I'm</p> <p>15 not asking you about results. I'm asking you</p> <p>16 about literature.</p> <p>17 A. And I'm telling you about the</p> <p>18 results that I see in the literature.</p> <p>19 Q. Okay.</p> <p>20 A. That there are results that stem</p> <p>21 from measuring the size of the trade or the</p> <p>22 size of the trade relative to volume versus</p> <p>23 there are other results that look at just</p> <p>24 whether someone is trading or whether there is</p> <p>25 a trade.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, let me ask you this</p> <p>3 question. I've been going through this</p> <p>4 material and going through the literature and</p> <p>5 this term "power" comes up.</p> <p>6 Can you tell me what the term</p> <p>7 "power" of a regression method is?</p> <p>8 A. Generally, the power of a</p> <p>9 regression is the ability to detect a</p> <p>10 relationship.</p> <p>11 Q. Okay. So that -- and do</p> <p>12 different analyses or methods have different</p> <p>13 powers?</p> <p>14 A. They may.</p> <p>15 Q. Okay. And didn't the literature</p> <p>16 that you reviewed indicate that a regression</p> <p>17 that includes the size of the transactions is</p> <p>18 of greater power than one that does not?</p> <p>19 A. I'm not aware of that.</p> <p>20 Q. You're not aware of any literature</p> <p>21 that says that?</p> <p>22 A. I'm not aware of that.</p> <p>23 Q. Okay. Now, the other is, is that</p> <p>24 on -- when you have the variable "any Rhino</p> <p>25 trading," that doesn't distinguish between</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. And that sells at the bids have a</p> <p>3 tendency to push the price down?</p> <p>4 A. Again, I don't think I've</p> <p>5 testified to that yet, but it's possible.</p> <p>6 Q. Okay. And that this doesn't --</p> <p>7 this analysis in Regression Number 1 doesn't</p> <p>8 take into consideration either of those facts,</p> <p>9 does it?</p> <p>10 MR. SOHN: Objection to form.</p> <p>11 A. It takes into account whether</p> <p>12 Rhino's buying and -- and/or selling.</p> <p>13 Q. It doesn't take into account, one,</p> <p>14 the size of the transactions. Correct?</p> <p>15 A. Correct.</p> <p>16 Q. And it doesn't take into</p> <p>17 consideration whether or not the buys or sells</p> <p>18 were bids or asks, does it?</p> <p>19 A. That's correct. It just looks at</p> <p>20 the overall effect.</p> <p>21 Q. Okay. Now, let's go to Regression</p> <p>22 Number 2. I'm sorry to keep coming back to it,</p> <p>23 but I am very puzzled by -- by how you've</p> <p>24 described the regression and how it's modeled.</p> <p>25 Does this regression take into</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 whether or not Rhino bought or Rhino sold, does</p> <p>3 it?</p> <p>4 A. No, it just looks at whether there</p> <p>5 -- there's an impact from Rhino being in the</p> <p>6 market.</p> <p>7 Q. So Rhino's in the market. It</p> <p>8 could go up or it could go down?</p> <p>9 A. Rhino's in the market. Is there</p> <p>10 an impact from Rhino being in the market on the</p> <p>11 stock price?</p> <p>12 Q. Okay. And it doesn't measure</p> <p>13 whether its activities are buy or sell. It's</p> <p>14 just in the market?</p> <p>15 A. It measures whether it's a buy and</p> <p>16 a sell.</p> <p>17 Q. Okay. Now, you indicated earlier,</p> <p>18 I thought, that buys at the offer, for example,</p> <p>19 could have a tendency of pushing the price up.</p> <p>20 MR. SOHN: Objection to form.</p> <p>21 A. I'm not sure if I testified to</p> <p>22 that. That might be the case.</p> <p>23 Q. Okay. You've seen literature to</p> <p>24 that effect, haven't you?</p> <p>25 A. I may have, yes.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 consideration the size of the buys or sells in</p> <p>3 determining the effect of a share price?</p> <p>4 MR. SOHN: Objection to form.</p> <p>5 A. No, it doesn't. It just takes</p> <p>6 into account whether there was a sell or</p> <p>7 whether there was a buy.</p> <p>8 Q. Now, Regression Number 3, it has</p> <p>9 these additional variables: The transfers and</p> <p>10 the principals, for example.</p> <p>11 And is there any evidence in the</p> <p>12 record of this case or in anything that's been</p> <p>13 provided to you that indicates either of those</p> <p>14 events was information that was publicly</p> <p>15 available?</p> <p>16 MR. SOHN: Objection to form.</p> <p>17 A. I haven't seen any specific</p> <p>18 evidence regarding whether that information was</p> <p>19 publicly available. I know it was available to</p> <p>20 the parties about what they were doing. And</p> <p>21 that's a flag to catch the effects of those</p> <p>22 variables -- of those -- of those transactions.</p> <p>23 Q. Well, isn't what your -- your</p> <p>24 regression doing is trying to determine what</p> <p>25 Badian's activity had on the price of Sedona in</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 the market?</p> <p>3 A. That's the overall objective of</p> <p>4 the entire statistical analysis, is to figure</p> <p>5 out if there is an impact from any kind of</p> <p>6 Rhino activity on the stock price.</p> <p>7 Q. Well, isn't it important to</p> <p>8 determine when you're modeling something</p> <p>9 whether that information was factored into the</p> <p>10 market by being publicly available?</p> <p>11 MR. SOHN: Objection to form.</p> <p>12 A. I don't think it's important. I</p> <p>13 don't think it's important to do that. I think</p> <p>14 it's important to check -- look at your</p> <p>15 analyses and make sure you're covering all your</p> <p>16 bases by checking to see if there is any impact</p> <p>17 on the market through transfers of principal</p> <p>18 transactions.</p> <p>19 Q. Well, isn't it correct to say that</p> <p>20 any analysis is only as good as the data on</p> <p>21 which it rests?</p> <p>22 MR. SOHN: Objection to form.</p> <p>23 A. I guess you want to have good</p> <p>24 data. You want to make sure your data are</p> <p>25 accurate.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, it was a general question,</p> <p>3 so I'm replying in a general sense.</p> <p>4 Q. So you're answering the question</p> <p>5 generally.</p> <p>6 Now, is it correct to say that to</p> <p>7 properly interpret the results of a regression</p> <p>8 that you need to understand the design of the</p> <p>9 study?</p> <p>10 A. To properly interpret the results</p> <p>11 of the regression, yeah, you want to understand</p> <p>12 the purpose of the analysis and the various</p> <p>13 different statistical analyses that are done to</p> <p>14 answer the question, which is the purpose of</p> <p>15 the analysis.</p> <p>16 Q. Okay. And isn't it also true that</p> <p>17 different designs can result in different</p> <p>18 answers?</p> <p>19 MR. SOHN: Objection to form.</p> <p>20 A. Different designs may result in</p> <p>21 different answers.</p> <p>22 Q. Okay. Now --</p> <p>23 A. That's what you're trying --</p> <p>24 that's why you try to cover all your bases, to</p> <p>25 make sure that you covered all your bases.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. What do you mean by "accurate"?</p> <p>3 A. Measuring what you think you're</p> <p>4 measuring accurately.</p> <p>5 Q. So, that, you want to make sure</p> <p>6 that the data is data that is data that might</p> <p>7 have an impact on what you're measuring?</p> <p>8 MR. SOHN: Object to the form.</p> <p>9 A. You want to make sure that, A, the</p> <p>10 data is correct. That the data series you're</p> <p>11 using or the database you're using is --</p> <p>12 accurately reflects the data that you think</p> <p>13 it's reflecting.</p> <p>14 Q. Okay.</p> <p>15 A. And, that, you want to use data</p> <p>16 that you think could potentially have an effect</p> <p>17 on the stock price, or variables that could</p> <p>18 potentially have an effect on the stock</p> <p>19 price.</p> <p>20 Q. And is it fair to say that the</p> <p>21 design of the study determines the quality of</p> <p>22 the output of that study?</p> <p>23 A. In a very general sense.</p> <p>24 Q. Is it -- what do you mean by "a</p> <p>25 general sense"?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. So, is it your position that the</p> <p>3 data selected and the variables selected for</p> <p>4 the independent variable has to be data that</p> <p>5 can possibly have an impact on the dependent</p> <p>6 variable, this being the movement of the Sedona</p> <p>7 stock price in this case?</p> <p>8 MR. SOHN: Objection to form.</p> <p>9 A. Yeah. In this matter you want to</p> <p>10 look at variables that potentially could have</p> <p>11 an impact on Sedona's stock price, whether they</p> <p>12 be buys, sells, transfers, principal. You want</p> <p>13 to -- you want to look at all of that, so all</p> <p>14 that could potentially have an effect on the</p> <p>15 stock price.</p> <p>16 Q. Could the validity of a regression</p> <p>17 analysis be undermined by the use of</p> <p>18 overinclusive data?</p> <p>19 A. I don't know what you mean by</p> <p>20 "overinclusive data."</p> <p>21 Q. Can a study be invalid because</p> <p>22 it's overinclusive?</p> <p>23 A. I don't know what you mean by</p> <p>24 "overinclusive."</p> <p>25 Q. Well, overinclusive in</p>

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<p>1 - STEPHEN D. PROWSE - 2 relationship to the impact on the dependent 3 variable that's being studied. 4 A. Sorry, that doesn't help. 5 Q. Remember my example of December of 6 '09 and December of '07, my hypothetical? 7 A. Barely. 8 Q. Do you recall that I asked you 9 whether or not what activity occurred in '07 10 and what the -- what -- what the usefulness of 11 that information would be in determining what 12 someone did in trading stock in December of 13 '09? 14 A. I think you used different dates, 15 but I remember the hypothetical, yes. 16 Q. Okay. Well, I used the full date 17 range. I'm just using the months now. 18 The -- is it your position that 19 you could select trading at any time during the 20 period of time Sedona stock was trading to 21 determine, for example, what happened in March 22 of 2001? 23 MR. SOHN: Objection to form. 24 A. It's my position that there are 25 two periods that you need to look at: One is</p>	<p>1 - STEPHEN D. PROWSE - 2 convertible debenture entered into? 3 A. November of 2000. 4 Q. Okay. And why did you include the 5 period before the convertible debenture even 6 existed -- 7 A. Because -- 8 Q. Excuse me. 9 -- if what's being measured is 10 activity that might be influenced by the 11 existence of that convertible debenture? 12 A. Because that includes a period in 13 which Rhino was trading and in which Rhino had 14 a previous FPS from Sedona. So I think it's 15 very reasonable to want to understand what 16 happened in that period, because that can tell 17 you some things about what happens in the 18 period after the issuance of the convertible G. 19 Q. Well, let's take that period. 20 Did you -- did you take a look to 21 see what the trading patterns were during the 22 period of time that was used to determine the 23 price at which Badian could convert into Sedona 24 stock from that preferred stock issuance? 25 MR. SOHN: Objection to form.</p>
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<p>1 - STEPHEN D. PROWSE - 2 the entire period over which Rhino trades, 3 because that's the entity -- entity that's the 4 focus of interest. You want to understand what 5 the data tells you about whatever price impacts 6 there are from Rhino's trading over the entire 7 time period that it trades. 8 And then, there's a second period 9 to look at, which is, I think, a reasonable 10 period to look at, which concentrates -- it 11 looks at a narrower period over which, you 12 know, there's a -- there's a number of 13 conversions. So I think those -- those are the 14 two appropriate reasonable periods to look at. 15 Q. Well, let's take the longer period 16 of time. What was the time period? June of 17 2000 through June of 2002? 18 A. June of two -- June 26, 2000 to 19 June 14, 2002. 20 Q. Now, this case involves 21 allegations of manipulating stock to gain an 22 advantage in converting a debenture into -- 23 into that stock. Right? 24 A. Right. 25 Q. Okay. When -- when was the</p>	<p>1 - STEPHEN D. PROWSE - 2 A. From which preferred stock 3 issuance? 4 Q. The preferred stock issuance that 5 existed, that it converted during that period 6 of time. 7 A. During what period of time? 8 Q. Prior to November 22nd of 2000. 9 A. I believe there was a conversion 10 period in there. I'm not sure where it was. 11 But if that is included in the date range that 12 we looked at, then we looked at it. 13 Q. Well, I mean, what I'm asking you 14 is, did you take a look at the time period, the 15 specific time period in which the conversion 16 was priced and compare it with anything else? 17 A. I think we have that data and I 18 think I've looked at it, but I can't remember 19 offhand what it tells you. 20 Q. Is it in the report? 21 A. No, it's not in the report. 22 Q. Now, subsequent to May 31st, okay, 23 were there any events that you know of that 24 might have had an impact on Badian's trading 25 strategy?</p>

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<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: 2001? 3 MR. GUIDO: 2001. 4 Q. After May 31st, 2001. 5 A. After May 31st, 2001. 6 Q. Uh-huh. 7 A. Yeah. Rhino still held a 8 significant position in the FPS. That didn't 9 go away until June of 2002. And, so, I think 10 that's legitimate to look at, too. 11 Q. Anybody ever show you an e-mail 12 from Andreas Badian to his brother that says 13 they obviously knew what they were doing was 14 wrong? 15 A. No. 16 Q. Never saw that? 17 A. Never saw that. 18 Q. Did anyone ever tell you that, in 19 October of 2001, sedona refused to honor a 20 conversion letter because it concluded that 21 Badian was engaged in manipulation of its 22 stock? 23 A. I may have. I can't recall if 24 I've -- I can't recall if I've -- I don't think 25 I've seen a document that tells me that. I</p>	<p>1 - STEPHEN D. PROWSE - 2 that's a disincentive? 3 MR. SOHN: Objection to form. 4 A. Well, I don't understand your 5 question. If you can point me to somewhere in 6 my report where you think I say that, I'd be 7 happy to look at it. 8 Q. The -- you said that you read 9 Beloreshki's report, "The Frontiers of 10 Convertible Financing." And that was one of 11 the things that you based your opinion on is 12 that you read the article. 13 A. I said I had read the article, 14 yes. 15 Q. Okay. Well, do you recall that in 16 the article he indicated that one of the 17 disincentives to market manipulation is that 18 there's what's called a litigation contract 19 renegotiation. 20 A. I remember that discussion, but I 21 don't remember the specifics of it. If you 22 want me to take a look at the article, I'd be 23 happy to do so. 24 Q. Why don't you take a look at 25 Exhibit No. 5.</p>
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<p>1 - STEPHEN D. PROWSE - 2 can't recall if I knew that at one point. 3 Q. But I think that when I asked you 4 questions about, you know, as an economist, you 5 know, what are cost benefits, I think one of 6 the things you indicated was that a person 7 might renege on their contractual obligations 8 based on manipulative stock trading. 9 MR. SOHN: Objection to form. 10 A. No, I certainly didn't say that. 11 Q. What did you say? 12 A. I said a person might renege on a 13 contractual provision if the economics for that 14 person works in a particular way. If a -- if a 15 contractual provision says I have to pay a 16 million dollars to somebody and I don't have 17 the million dollars, well, I may have to -- I 18 may have to breach the contract. 19 So, you know, there's something 20 known as efficient breach. But I certainly 21 didn't say what you said I said. 22 Q. Well, I think that in your paper, 23 in your expert report, you talk about how there 24 are disincentives to market manipulation. Or 25 am I wrong that you don't really think that</p>	<p>1 - STEPHEN D. PROWSE - 2 MR. SOHN: Five? 3 MR. GUIDO: Five. 4 Q. And I direct your attention to 5 page 7, item number 4. 6 A. I see that. 7 Q. So one of the risks of -- that one 8 has to weigh is the litigation or contract 9 renegotiation risk when one chooses to try and 10 manipulate the stock price. 11 MR. SOHN: Is that a question? 12 A. I don't see any reference to 13 manipulating a company's stock in here. 14 Q. Does it talk about litigation 15 risks with the issuer if the issuer is unhappy 16 about how the purchaser of a future price 17 security has acted? 18 MR. SOHN: Is that a question? 19 A. It -- it does talk about 20 litigation risks in the third paragraph of that 21 section. 22 Q. Now let's turn to your -- the 23 report that you signed. We'll start with page 24 5. We haven't talked about the risk/return 25 profile that you have here.</p>

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<p>1 - STEPHEN D. PROWSE - 2 Do you have the report in front of 3 you? Look at paragraph 18. 4 MR. SOHN: Mr. Guido, can we take 5 a break at a convenient moment? 6 MR. GUIDO: Sure. Five-minute 7 break? 8 MR. SOHN: Yes, thank you. 9 MS. SCHECHTMAN: Yes. 10 THE VIDEOGRAPHER: Going off the 11 record at 3:21 p.m. 12 (A recess is taken.) 13 THE VIDEOGRAPHER: Going back on 14 the record at 3:32 p.m. 15 BY MR. GUIDO: 16 Q. If you were asked to evaluate the 17 models that were used for these regressions as 18 an expert, what questions would you ask as to 19 whether or not the models were appropriate? 20 MR. SOHN: Objection to form. 21 A. I would ask whether -- whether 22 there was a -- I would look to see whether 23 there was a potential that the variables that 24 were being used as independent variables could 25 affect -- could be -- potentially affect</p>	<p>1 - STEPHEN D. PROWSE - 2 Is there a potential for the 3 variables that you're looking at to have an 4 effect on Sedona's stock price? 5 Q. Well, is the -- the weight of the 6 variables, is that a relevant question to ask 7 about whether or not the model is appropriately 8 created? 9 A. I don't know what you mean by "the 10 weight of the variables." 11 Q. Well, I mean you can -- you can 12 say trading or not trading. Okay? That's a 13 potential to have an impact. Correct? 14 A. I agree. 15 Q. Okay. And the -- the size of the 16 trading or the frequency of the trading on a 17 particular day could also be a relevant factor, 18 could it not? 19 A. The side of the trade could be. 20 Q. Anything else? 21 A. Well, that's what I'm saying. You 22 want to -- you want to look at variables -- you 23 want to look at your measures and see if they 24 all have a potential to affect the stock price. 25 Q. Okay. Is the size of the trading</p>
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<p>1 - STEPHEN D. PROWSE - 2 Sedona's stock price. 3 Q. Anything else? 4 A. Could you repeat the question or 5 have it read back? 6 (Whereupon, the record is read 7 back.) 8 A. I mean, I think that would be the 9 basic question. 10 Q. Any others? 11 A. Well, I might have to -- there 12 might have -- there might be some with regards 13 to the particular specifications of the 14 variables. 15 Q. I'm sorry, the -- 16 A. The particular specifications or 17 combinations of the variables. But I think 18 that's the -- that's the main question from 19 a -- from a -- from -- if the question is with 20 regards to what -- what -- given that you think 21 the regression analysis is appropriate, and in 22 this setting, and what the -- what the proper 23 independent variables should be that you should 24 look at, then I think that's the main -- the 25 main answer.</p>	<p>1 - STEPHEN D. PROWSE - 2 in relationship to the size of the market a 3 variable that you would think to include in an 4 appropriately structured model? 5 A. That's a potential variable that 6 you should look at, and we did. 7 Q. So those are the -- those are the 8 factors that you would look to to decide 9 whether or not these models were appropriately 10 structured? 11 MR. SOHN: Objection to the form. 12 A. Right. Are they independent 13 variables? Do they have a potential to affect 14 Sedona's stock price? 15 Q. So one is whether selling exists 16 or doesn't exist, or buying exists or buying 17 doesn't exist. That's one. 18 Whether the -- whether size of the 19 sales or the buys have an impact? 20 A. Correct. 21 Q. Whether the size in relationship 22 to other participants' behavior in the market 23 have an impact? 24 A. Can you say that again? 25 Q. The size and relationship to other</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 participants' activity in the marketplace.</p> <p>3 A. Yes. Yes, that's -- that's a</p> <p>4 potential variable.</p> <p>5 Q. Now, when you did your analysis,</p> <p>6 did the data include sales by Pond into the</p> <p>7 market?</p> <p>8 A. The data that we used came from</p> <p>9 the account statements. So to the extent that</p> <p>10 Rhino trades were executed through Pond, that</p> <p>11 was included in the data.</p> <p>12 Q. Meaning Rhino's sales to Pond were</p> <p>13 reported in the data?</p> <p>14 A. To the -- to the extent that</p> <p>15 Rhino's trades were executed through -- by</p> <p>16 Pond, that was included in the data.</p> <p>17 Q. Well, is the data of Pond sales to</p> <p>18 the market in the database?</p> <p>19 A. The database is constructed to</p> <p>20 look at data -- to look at Rhino's transactions</p> <p>21 as reported in Rhino's account statements.</p> <p>22 Q. Okay.</p> <p>23 A. So all of the account statement</p> <p>24 data is in our -- is in our database.</p> <p>25 Q. Are you aware that the Rhino sales</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 That data was, I understand,</p> <p>3 validated with NERA and edited at some point in</p> <p>4 time by reference to documents Bates stamped</p> <p>5 GOJO and RA, which I understand are account</p> <p>6 statements and bank statements.</p> <p>7 That database, that electronic</p> <p>8 database, was a database that Mr. Beloreshki</p> <p>9 took with him when he left NERA on CD and</p> <p>10 stayed with him until he came to FTI. So that</p> <p>11 was the data that we used when doing the</p> <p>12 analysis on our report that is reported in</p> <p>13 our -- in our report.</p> <p>14 The -- subsequently, when we did</p> <p>15 our report, we didn't have the source documents</p> <p>16 at FTI that went into creating the electronic</p> <p>17 database. But based on my conversations with</p> <p>18 Mr. Beloreshki, I had a high confidence in the</p> <p>19 accuracy and the precision of the data.</p> <p>20 Subsequent to issuing our report,</p> <p>21 we have now received all of the account</p> <p>22 statements, all of the RA Bates document</p> <p>23 statements, all of the GOJO Bates document</p> <p>24 statements, all of the R statements, that we</p> <p>25 have now since gone back and validated the</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 in March and Badian sales to Refco were</p> <p>3 executed by Pond?</p> <p>4 MR. SOHN: Objection to form.</p> <p>5 A. I can't recall the specifics.</p> <p>6 That might be the case.</p> <p>7 Q. But you don't know?</p> <p>8 A. I don't know for certain without</p> <p>9 looking at the data.</p> <p>10 Q. Well, does the data that you</p> <p>11 claimed to have looked at, does that include</p> <p>12 sales by Pond?</p> <p>13 A. To the extent that sales by Pond</p> <p>14 came from Rhino transactions as reported in</p> <p>15 Rhino's account statements, yes.</p> <p>16 Q. Well, how was the data</p> <p>17 constructed?</p> <p>18 A. My understanding is the data was</p> <p>19 constructed in the following manner, that --</p> <p>20 that we're using in this manner: Prior to</p> <p>21 FTI's engagement in this matter, I understand</p> <p>22 an electronic database was constructed by NERA</p> <p>23 using account statements from accounts such as</p> <p>24 Westminster, Amro, Refco, brokerages such as</p> <p>25 Westminster and others.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 electronic database that we used for the</p> <p>3 analysis in our initial report.</p> <p>4 And we made -- we found a number</p> <p>5 of changes that we had to take. They were all</p> <p>6 minor, I would say. Most of them had to do</p> <p>7 with nonmarket transfers on dates outside,</p> <p>8 dates either in 2000 or in 2002. There were a</p> <p>9 couple of market transactions that were --</p> <p>10 there was one market transaction that was off</p> <p>11 by a day, and I think there were a couple of</p> <p>12 market transactions that were buys and sells on</p> <p>13 the same days or subsequent days that were</p> <p>14 actually canceled.</p> <p>15 But after making -- but after</p> <p>16 making those edits subsequent to issuing our</p> <p>17 report, we -- we now have a database that we</p> <p>18 think is as validated as it can be. And we've,</p> <p>19 since issuing our report, rerun all our</p> <p>20 statistical analyses that we did and nothing</p> <p>21 changed from the results we -- our opinions</p> <p>22 don't change. There may have been small</p> <p>23 changes in the coefficients, but there were no</p> <p>24 changes in anything of importance.</p> <p>25 So our conclusions remain the same</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 after we validated the data using the source</p> <p>3 documents.</p> <p>4 Q. So, you've gone back and you've</p> <p>5 determined what the basis of the database was.</p> <p>6 Last night I received, at eight</p> <p>7 o'clock, a supplemental document production</p> <p>8 that includes the documents that are Bates</p> <p>9 stamped GOJO.</p> <p>10 A. Yes.</p> <p>11 Q. Is that the data -- is that the</p> <p>12 universe of the account statements that you</p> <p>13 used to verify the accuracy of the database?</p> <p>14 A. Yes. We received last night those</p> <p>15 documents, too.</p> <p>16 Q. Okay. Let me -- let me just sort</p> <p>17 of read through them, see whether or not</p> <p>18 there's something missing in what I have based</p> <p>19 on what you recall.</p> <p>20 There was an account called</p> <p>21 Cambois Finance of Westminster. Do you recall</p> <p>22 that account?</p> <p>23 A. I recall the name "Cambois."</p> <p>24 Q. Okay. And was that one of the --</p> <p>25 one of the accounts with trades that you</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. And what about an account BNC Bach</p> <p>3 International and an entity called Dundee?</p> <p>4 A. I believe that's in the database.</p> <p>5 Q. Any other?</p> <p>6 A. Not that I can remember off the</p> <p>7 top of my head.</p> <p>8 Q. This is all that I received.</p> <p>9 A. Those -- all -- all those names</p> <p>10 ring a bell with me.</p> <p>11 Q. Okay. Well, did you look at any</p> <p>12 Pond trade tickets?</p> <p>13 A. We did not look at any Pond trade</p> <p>14 tickets.</p> <p>15 Q. And did you look at any Pond</p> <p>16 account statements?</p> <p>17 A. I'm not sure. I know Pond was a</p> <p>18 broker for a lot of the transactions. So to</p> <p>19 the extent that the trades, the Rhino trades,</p> <p>20 went through Pond as a broker, then they would</p> <p>21 be in the database.</p> <p>22 Q. Are you sure of that? Because</p> <p>23 when I looked at the columns in the database,</p> <p>24 it doesn't include a column for Pond.</p> <p>25 A. Well, my understanding is that</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 included in your analysis?</p> <p>3 A. I believe so, yes.</p> <p>4 Q. Okay. Does that also apply to an</p> <p>5 account at Westminster for an entity called</p> <p>6 Roseworth Group?</p> <p>7 A. I believe so, yes.</p> <p>8 Q. Does that also include an account</p> <p>9 for Amro International and an entity called</p> <p>10 Refco Capital Markets?</p> <p>11 A. I'm not certain about that now,</p> <p>12 but I think so, but I'm not certain just</p> <p>13 sitting here.</p> <p>14 Q. What about a company called BNC</p> <p>15 Bach International and a broker called Rampart?</p> <p>16 A. Those -- those trades are</p> <p>17 included, my understanding, yes.</p> <p>18 Q. And what about an account in Amro</p> <p>19 International and Westminster?</p> <p>20 A. I understand that those dat --</p> <p>21 that data is in the database.</p> <p>22 Q. And what about an account BNC Bach</p> <p>23 International and Canaccord?</p> <p>24 A. I understand that's in the</p> <p>25 database.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Pond was a -- a broker through which some of</p> <p>3 Rhino's trades were made. And we -- my</p> <p>4 understanding is we have the -- the entire</p> <p>5 universe of Rhino trades regardless of who they</p> <p>6 were actually trading through.</p> <p>7 So to the extent that any Rhino</p> <p>8 trades went through Pond in some manner, we</p> <p>9 have those in our database. Now, if there are</p> <p>10 Pond trades that are coming from some other</p> <p>11 non-Rhino entity, then that -- that is not a</p> <p>12 defendant in this matter, we wouldn't have</p> <p>13 that.</p> <p>14 Q. Well, I'm talking about</p> <p>15 transactions that were transactions that were</p> <p>16 initiated by Badian and that they were pre --</p> <p>17 they were initiated that Pond executed into the</p> <p>18 market.</p> <p>19 Are those transactions included in</p> <p>20 your database?</p> <p>21 A. Any Rhino transaction -- my</p> <p>22 understanding is we have the universe of all</p> <p>23 Rhino transactions. So if there is a Rhino</p> <p>24 transaction that goes through Pond in some</p> <p>25 manner, then that is in our database.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Is every aspect of that reported</p> <p>3 transaction included in your database?</p> <p>4 A. Well, I don't know what you mean</p> <p>5 about "every aspect." We have -- I think -- I</p> <p>6 believe we have the price and I believe we have</p> <p>7 the number of shares and whether it was a buy</p> <p>8 or a sell. And I believe we have -- we</p> <p>9 obviously have the date of the trade. So if</p> <p>10 that's what you mean, yes.</p> <p>11 Q. I want you to take a look at</p> <p>12 documents that have been marked in this action</p> <p>13 as Exhibits 86 through 90.</p> <p>14 MR. GUIDO: They're in reverse</p> <p>15 order, Josh, so switch them.</p> <p>16 Josh, can you make life easier for</p> <p>17 me and pick a copy out of here for yourself?</p> <p>18 One of the things I like is, in</p> <p>19 the index, to do a listing of the old exhibits</p> <p>20 and where they first appeared in the</p> <p>21 transcript.</p> <p>22 BY MR. GUIDO:</p> <p>23 Q. While Mr. Sohn is pulling the</p> <p>24 exhibits, why don't you take a look at the</p> <p>25 packet.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 transactions in Sedona stock at Badian's</p> <p>3 request?</p> <p>4 A. I just don't know one way or the</p> <p>5 other.</p> <p>6 Q. I'd like you to take a look at the</p> <p>7 exhibit -- well, first of all, these are</p> <p>8 account statements based on the testimony of</p> <p>9 Mr. Spinner of a proprietary account that he</p> <p>10 managed at Pond in which he executed trades on</p> <p>11 behalf of Amro into the market.</p> <p>12 And my question is, have you ever</p> <p>13 seen Exhibits 86 through 90?</p> <p>14 A. I can't recall seeing them.</p> <p>15 Q. Is any of the data in 86 through</p> <p>16 90 included in your database?</p> <p>17 A. Based on my understanding of the</p> <p>18 data, if these are Rhino/Amro trades, if some</p> <p>19 of these are Rhino and Amro trades, those</p> <p>20 trades would be in our database. Because we</p> <p>21 have all the -- my understanding is we have all</p> <p>22 the data for Rhino's transactions.</p> <p>23 Q. Well, in your document production,</p> <p>24 I mean, look in your exhibit -- your exhibit --</p> <p>25 I can't remember if it's two or three, where</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 MR. SOHN: Can we take the others</p> <p>3 out? Can we take one more?</p> <p>4 MR. GUIDO: I can only let you</p> <p>5 have one.</p> <p>6 MR. SOHN: Come on, Ken.</p> <p>7 MR. GUIDO: They're only</p> <p>8 accompanying you. I heard you introduce them.</p> <p>9 BY MR. GUIDO:</p> <p>10 Q. Have you ever heard the name "Jake</p> <p>11 Spinner"?</p> <p>12 A. Yes.</p> <p>13 Q. Who is Jake Spinner?</p> <p>14 A. Who is Jake Spinner?</p> <p>15 Q. Yeah.</p> <p>16 A. I believe he's a defendant in this</p> <p>17 matter.</p> <p>18 Q. Do you know what his role was</p> <p>19 in -- in this matter?</p> <p>20 A. I believe he was at Pond Equities</p> <p>21 and his role is described in the Complaint. I</p> <p>22 can't give you the details, but I'd be happy to</p> <p>23 look at the Complaint, if you'd like.</p> <p>24 Q. Well, was he the broker at Refco</p> <p>25 that was responsible for the execution of the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 you describe --</p> <p>3 A. Three.</p> <p>4 Q. -- what it is you looked at.</p> <p>5 A. Three.</p> <p>6 Q. Do you see any mention of these</p> <p>7 Pond trade tickets in these account statements?</p> <p>8 A. No.</p> <p>9 Q. So you didn't use them?</p> <p>10 A. No, I have already described how</p> <p>11 the data -- I understand the database to be</p> <p>12 constructed.</p> <p>13 Q. Well --</p> <p>14 A. Five minutes ago.</p> <p>15 Q. I understand that. And we went</p> <p>16 through the list of how the database was</p> <p>17 constructed, did we not?</p> <p>18 A. Went through the list? I'm not</p> <p>19 sure what list --</p> <p>20 MR. SOHN: Objection to form.</p> <p>21 Q. Well, I asked you, based on what</p> <p>22 was provided to me last night, which you</p> <p>23 indicated you probably received a copy of what</p> <p>24 I received last night at eight o'clock, that --</p> <p>25 that in that -- that is the universe of</p>

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<p>1 - STEPHEN D. PROWSE - 2 information that went into your database. 3 A. The GOJO documents are an input 4 into the database, but my understanding is 5 there are also RA Bates stamped documents and 6 maybe some R stamped documents that are also 7 inputs into the database. So it's a 8 combination of those three documents which, in 9 their entirety, my understanding is, covers all 10 the account statements or trading activity of 11 Rhino. 12 Q. Well, in the Exhibits 86 through 13 90, do you see any RA Bates stamp numbers on 14 those? 15 A. No. 16 Q. But those documents have never 17 been Bates stamped RA, have they? 18 MR. SOHN: Objection. 19 Q. To your knowledge. 20 A. I don't know how I would know 21 that. 22 Q. Okay. So, are you aware that 23 transactions were initiated by Mr. Badian by 24 making calls to a man named Danny Graham, who 25 then called a man named Cliff About at Pond,</p>	<p>1 - STEPHEN D. PROWSE - 2 of that. 3 Q. Now, in your exhibit, the -- you 4 indicate that you looked at audit trail 5 reports? 6 A. Yes. 7 Q. Did you notice anything out of the 8 ordinary in the audit trail reports? 9 A. I don't know what you mean by "out 10 of the ordinary." They're thick reports about 11 that thick. So, we looked at them. We noted 12 what they were. We understood what they were 13 based on the SEC's description of them in your 14 response to interrogatories, but that's the 15 extent of my knowledge. 16 Q. Well, did you read the responses 17 to the interrogatories? 18 A. Yes. 19 Q. And did you see in the responses 20 to the interrogatories that described certain 21 highlighting on those audit trail reports? 22 A. Yes, blue highlighting, yellow 23 highlighting, pink and orange, I believe. 24 Something like that. 25 Q. And did you see in those responses</p>
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<p>1 - STEPHEN D. PROWSE - 2 and that Cliff About then executed the trades 3 into the market. And at the end of the day, 4 Cliff About and Danny Graham got together and 5 they decided what number of shares Refco should 6 sell to Pond to cover Pond's sales into the 7 market. 8 Are you aware of that? 9 MR. SOHN: Objection to form. 10 A. To the extent that's in the -- 11 that description is in the Complaint, I'm aware 12 of that. 13 Q. Other than in the Complaint? 14 A. No. 15 Q. Are you aware that the 16 transactions that are reflected in Exhibit Nos. 17 86 through 90 involving Sedona's shares were 18 reported to the market? 19 A. I don't know if they were reported 20 to the market or not. 21 Q. Are you aware that the Refco sales 22 to Pond -- out of the Amro account to the Pond 23 proprietary account managed by Mr. Spinner were 24 reported to the market? 25 A. I'm not aware one way or the other</p>	<p>1 - STEPHEN D. PROWSE - 2 to the interrogatories it explained the 3 significance of those highlights? 4 A. It did give a definition of what 5 the highlights meant, yes. 6 Q. And did you also, when you looked 7 at that interrogatory response, see it included 8 within the interrogatory responses was a 9 description from FINRA of what the columns 10 meant in the audit trail report? 11 A. I believe I saw that. 12 Q. Okay. Did you make an effort to 13 determine which of the highlighted trades had 14 been reported to the market? 15 A. No, we did not do that. 16 Q. Okay. So you don't know whether 17 or not the Pond trades in Exhibit 86 through 90 18 were reported to the market? 19 A. We didn't do that analysis. 20 Q. Okay. And you don't know whether 21 the Refco to Pond transactions that were 22 reflected in that -- in those audit trail 23 reports were reported to the market? 24 A. We didn't do that analysis. 25 Q. Okay. Did you include in your</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 analysis both the Pond trades into the market,</p> <p>3 the sales into the market, and Refco's sales to</p> <p>4 Pond in your analysis?</p> <p>5 A. We accounted -- in our database,</p> <p>6 we analyzed Rhino's trades; buys, sells and</p> <p>7 other transactions. To the extent that they</p> <p>8 are covered by your descriptions, we -- they</p> <p>9 are in our database.</p> <p>10 Q. Are you sure of that?</p> <p>11 A. I'm -- I mean, that's my</p> <p>12 understanding; that we have the universe of</p> <p>13 Rhino's trades, regardless of who they went</p> <p>14 through, and transactions. And to the extent</p> <p>15 that's true, then we have everything that Rhino</p> <p>16 did regardless of who it's through.</p> <p>17 Q. So you're saying in your database,</p> <p>18 if I went back and looked at it, is that every</p> <p>19 trade, every transaction involved a sell by</p> <p>20 Amro, out of an Amro-related account, that</p> <p>21 every aspect of that transaction, if it was</p> <p>22 reported to the market, would be included in</p> <p>23 your database?</p> <p>24 MR. SOHN: Objection to the form.</p> <p>25 A. Well, I'm not sure what you mean</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. If all of Rhino's trades and</p> <p>3 transactions were not in our database? Then</p> <p>4 that's something that I'd want to investigate</p> <p>5 to see to what extent that database is not</p> <p>6 capturing Rhino trading activity and when</p> <p>7 was -- and for what period of time. And we'd</p> <p>8 obviously want to look at that and understand</p> <p>9 why that's happening and try and -- try and</p> <p>10 adjust for that.</p> <p>11 MR. GUIDO: I think one of the</p> <p>12 exhibits that I showed Mr. Beloreshki is in the</p> <p>13 originals. It's the 21A report.</p> <p>14 Could you show that to the witness,</p> <p>15 please?</p> <p>16 MR. SOHN: Exhibit 10.</p> <p>17 BY MR. GUIDO:</p> <p>18 Q. In Exhibit 10, which was</p> <p>19 previously called the 21A report, it was filed</p> <p>20 by Rhino in this case. There's attached at the</p> <p>21 end of it a schedule of transactions that I</p> <p>22 think is referred to as Exhibit D in that.</p> <p>23 A. Yeah, I have it.</p> <p>24 Q. Does that look familiar to the</p> <p>25 electronic database that you indicated that you</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 by "every aspect" of that trade. If you mean</p> <p>3 the number of shares, whether it was a buy or a</p> <p>4 sell, the day on which it occurred, yes, all</p> <p>5 that would be in the database.</p> <p>6 Q. Well, assume this hypothetical:</p> <p>7 Assume that Andreas instructed Rhino to sell</p> <p>8 out of the Amro account stock to Pond,</p> <p>9 proprietary accounts that was run by Spinner.</p> <p>10 And he instructed Spinner to sell out of that</p> <p>11 account into the market the Sedona shares. And</p> <p>12 that he instructed both of those transactions</p> <p>13 to be reported to the market. Just take that</p> <p>14 as an assumption.</p> <p>15 Would both of those transactions</p> <p>16 be included in your database?</p> <p>17 MR. SOHN: Objection.</p> <p>18 A. I believe so. I'd have to -- I</p> <p>19 could check, but my assumption -- my</p> <p>20 understanding is that all Rhino trades and</p> <p>21 transactions are included in our database.</p> <p>22 Q. If they were not -- assume that</p> <p>23 that hypothetical is true. If they were not,</p> <p>24 would your database be inaccurate?</p> <p>25 MR. SOHN: Objection to form.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 saw had been created in NERA?</p> <p>3 MR. SOHN: Objection to the form.</p> <p>4 A. Well, obviously I can't testify as</p> <p>5 to the numbers because I don't have the</p> <p>6 electronic database to compare to, but some of</p> <p>7 the first -- the first four columns are similar</p> <p>8 in that that information is in our electronic</p> <p>9 database. The trade date, the buy/sell total</p> <p>10 and the cumulative -- the quantity total and</p> <p>11 the cumulative quantity total. Those are --</p> <p>12 those are columns that are also in our</p> <p>13 electronic database.</p> <p>14 Q. And there are columns for</p> <p>15 different brokerage accounts also in your</p> <p>16 database. Isn't that correct?</p> <p>17 A. I believe that is correct. I'm</p> <p>18 not entirely certain.</p> <p>19 Q. Well --</p> <p>20 A. I know there is a -- I know there</p> <p>21 is a summary, a spreadsheet, that I'm familiar</p> <p>22 with that sums everything up for all accounts,</p> <p>23 brokerages, whatever.</p> <p>24 Q. I mean, that's the first three</p> <p>25 column in the spreadsheet, the aggregate data?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Right. And that's what I was</p> <p>3 referring to. That's the data I'm familiar</p> <p>4 with.</p> <p>5 Q. But with regard to the data, have</p> <p>6 you seen any spreadsheets that have columns for</p> <p>7 transactions in the account at Pond Equities in</p> <p>8 which Jake Spinner had traded in?</p> <p>9 A. I just don't know.</p> <p>10 Q. Well, did you see in the database</p> <p>11 any equity that said "Pond Equities"?</p> <p>12 A. I can't remember seeing anything</p> <p>13 that said "Pond." That doesn't mean it's not</p> <p>14 there, but I can't remember seeing it. And</p> <p>15 that doesn't -- that doesn't mean it might not</p> <p>16 be covered by something else. I just don't</p> <p>17 know.</p> <p>18 Q. Well, I understand that, but I'm</p> <p>19 just asking if there's anything in the database</p> <p>20 that you saw, anything that said "Pond</p> <p>21 Equities" in the database. And you don't</p> <p>22 recall seeing any?</p> <p>23 A. I don't recall.</p> <p>24 Q. Well, in Exhibit No. 3, the</p> <p>25 documents you looked through, that also doesn't</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Prowse. Going back on the record at 4:23 p.m.</p> <p>3 BY MR. GUIDO:</p> <p>4 Q. I hand you the document I've had</p> <p>5 marked as BP-25.</p> <p>6 Do you recognize that document?</p> <p>7 A. No, I don't.</p> <p>8 Q. Do you recall that you prepared a</p> <p>9 set of notes reflecting your understanding of</p> <p>10 the Pet Quarters issues?</p> <p>11 MR. SOHN: Objection to form.</p> <p>12 A. I don't recall preparing any</p> <p>13 notes, and I don't believe these are my notes.</p> <p>14 Q. Is there anybody at FTI with the</p> <p>15 initials DS that worked on the Pet Quarters</p> <p>16 matter?</p> <p>17 A. No. I don't -- I don't know what</p> <p>18 DS stands for.</p> <p>19 Q. Okay. Look under "Government</p> <p>20 Theories." You see Number 2, "Manipulation</p> <p>21 pattern: (i) depress stock price by showing</p> <p>22 store; (ii) submit conversion notice; (iii)</p> <p>23 engage in wash sales in order to enhance</p> <p>24 liquidity and artificially inflate the stock</p> <p>25 price"? Do you see that?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 make any mention to the account statements that</p> <p>3 I've shown you that have been marked as</p> <p>4 Exhibits 86 through 90, has it?</p> <p>5 A. That's correct.</p> <p>6 Q. And the list of GOJO account</p> <p>7 statements which were provided to me at eight</p> <p>8 o'clock last night, those also don't include</p> <p>9 any reference to Pond Equities accounts, do</p> <p>10 they?</p> <p>11 A. I haven't gone through all the</p> <p>12 GOJO documents, so I can't say one way or the</p> <p>13 other.</p> <p>14 MR. GUIDO: All right. Let's take</p> <p>15 a break.</p> <p>16 THE VIDEOGRAPHER: This concludes</p> <p>17 Tape Number 3 in the videotaped deposition of</p> <p>18 Dr. Stephen Prowse. Going off the record at</p> <p>19 4:09 p.m.</p> <p>20 (A recess is taken.)</p> <p>21 (Whereupon, exhibit is received</p> <p>22 and marked BP-25 for identification.)</p> <p>23 THE VIDEOGRAPHER: This begins</p> <p>24 Tape Number 3 -- or, excuse me, Tape Number 4</p> <p>25 in the videotaped deposition of Dr. Stephen</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Yes.</p> <p>3 Q. Now, does that control, to your</p> <p>4 understanding, the Complaint in this case?</p> <p>5 MR. SOHN: Objection to the form.</p> <p>6 A. I think that -- I think that could</p> <p>7 be close, yeah.</p> <p>8 Q. Now, the -- now, did you do an</p> <p>9 evaluation of wash sales to see whether or not</p> <p>10 they enhanced liquidity and artificially</p> <p>11 inflated the Sedona stock price in your</p> <p>12 analysis?</p> <p>13 MR. SOHN: Objection to form.</p> <p>14 A. We did analyze the wash sales to</p> <p>15 the -- because they were part of the data that</p> <p>16 we looked at.</p> <p>17 Q. Okay.</p> <p>18 A. So --</p> <p>19 Q. Did you separate them out to</p> <p>20 anyone?</p> <p>21 MR. SOHN: Objection; asked and</p> <p>22 answered.</p> <p>23 A. We did not separate them out.</p> <p>24 They were part of the entire analysis.</p> <p>25 Q. Remember I showed you the</p>

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<p>1 - STEPHEN D. PROWSE - 2 exhibit -- the rebuttal report from Pet 3 Quarters? And it had an exhibit at the end of 4 it. It did an analysis of those, of the trades 5 in Pet Quarters. 6 A. Some trades in Pet Quarters, 7 correct. 8 Q. Some trades. The Westminster/ 9 Amro-related accounts and the Refco/Amro- 10 related accounts. Remember that? 11 A. I'm not sure they were all 12 Westminster/Refco. I think some of them might 13 have been, but not all of them. 14 Q. But they were trades between 15 related entities? 16 A. I think that's right. 17 Q. And you recall that you did an 18 analysis to determine whether or not they 19 are -- how close they were to the offer or they 20 bid or somewhere in between? 21 A. Correct. 22 Q. And did you do such an analysis 23 with regard to the Sedona matter? 24 A. We did not do that analysis in 25 this matter.</p>	<p>1 - STEPHEN D. PROWSE - 2 price movements of Sedona. But it -- but it 3 wasn't just the characteristics of the 4 security. It was also the characteristics of 5 Sedona that made this an optimal trading 6 strategy -- or economically rational optimal 7 trading strategy. 8 Q. But just talking about the 9 debenture in the agreement itself. 10 So that one of them was that it 11 had a convert -- a floating conversion price. 12 A. Correct. 13 Q. That was one of the factors -- 14 A. Correct. 15 Q. -- to be considered? 16 A. Right. 17 Q. And that it was a debt instrument 18 in which Sedona's financial condition presented 19 a risk. Is that fair? 20 A. That's correct. The fact that it 21 was a debt instrument; the fact that it was a 22 risky security. For a variety of reasons. The 23 fact that there was a floating conversion 24 price. Those were the -- there was a lockup 25 period. Those were the characteristics --</p>
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<p>1 - STEPHEN D. PROWSE - 2 Q. Now, this -- I want to go page 5 3 where you talk of the risk/return profile and 4 what a rational trading strategy is. 5 MR. SOHN: Page 5 of Exhibit 4. 6 Correct? 7 MR. GUIDO: Page 5 of Exhibit 4. 8 MR. SOHN: Thank you. 9 BY MR. GUIDO: 10 Q. The -- in paragraph 18, you talk 11 about what's an economically rational and 12 beneficial trading strategy for holders of such 13 debentures; i.e., the Sedona November -- I 14 think it's November 22nd, 2000 debenture. 15 And what is your understanding of 16 the provisions of that debenture that were 17 relevant for your determination of whether or 18 not Badian had engaged in an economically 19 rational and beneficial trading strategy? 20 MR. SOHN: Objection to form. 21 A. Well, there were -- the provisions 22 that made it an FPS, for example; that there 23 would be a conversion price -- that there would 24 be a right to convert based on a floating 25 conversion price that was linked to the stock</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. What's a lockup period? 3 A. A period over which after 4 issuing -- after issuance of the FPS, the 5 investor is not allowed to convert. 6 Q. Not allowed to convert. 7 And there was a lockup period 8 here? 9 A. Yeah. 10 Q. What did that -- what was the 11 language of that lockup period? 12 A. I can't remember the lockup period 13 language, but -- sitting here. 14 Q. What was the lockup period? 15 A. I think it was three months. 16 Q. What time period to what time 17 period? 18 A. November 22nd, I believe, to March 19 22nd, I believe, of 2001. 20 Q. Was one of the other risks of the 21 instrument that it had a provision in it that 22 prohibited short sales? 23 A. Well, I wouldn't say that was a 24 risk. That was a provision that increased the 25 riskiness of the -- of the security.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. That was a lockup period, wasn't</p> <p>3 it? I mean, you could interpret it that way,</p> <p>4 couldn't you?</p> <p>5 A. I interpret a lockup period</p> <p>6 meaning that's the period over which your --</p> <p>7 you can't convert. The company won't honor a</p> <p>8 conversion notice.</p> <p>9 Q. I mean, it's -- I mean, in future</p> <p>10 price securities, is one of the issues that is</p> <p>11 discussed in the negotiations the limitations</p> <p>12 on the ability to convert?</p> <p>13 A. Absolutely. That's one of many</p> <p>14 different contract provisions that are</p> <p>15 negotiated between the parties, including the</p> <p>16 discount; whether there is a lockup period and</p> <p>17 the length of it; obviously the amounts.</p> <p>18 The -- various other contractual provisions are</p> <p>19 all negotiated.</p> <p>20 Q. Floors under conversion prices?</p> <p>21 A. You can have floors, you can have</p> <p>22 caps. Yes.</p> <p>23 Q. And do those affect the interest</p> <p>24 rate that a purchaser would request in its</p> <p>25 negotiations?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 MR. SOHN: Objection to form.</p> <p>3 A. Yeah.</p> <p>4 Q. Well, it says "reduce their</p> <p>5 overall long position in the underlying equity</p> <p>6 whenever possible." Okay?</p> <p>7 A. Correct.</p> <p>8 Q. And then "extend the period in</p> <p>9 which such positions were unwound."</p> <p>10 I mean, why are those -- I mean,</p> <p>11 if you say whenever possible, doesn't that mean</p> <p>12 as soon as possible?</p> <p>13 A. Yes.</p> <p>14 Q. And then --</p> <p>15 A. As soon as -- as soon as -- start</p> <p>16 as soon as possible and unwind -- and unwind</p> <p>17 your long position in the FPS or the underlying</p> <p>18 equity by shorting the stock and -- until the</p> <p>19 conversion period and then convert.</p> <p>20 Q. I'm sorry. I'm just looking at</p> <p>21 this. I'm trying to understand what this</p> <p>22 sentence means, not what you just said.</p> <p>23 A. Well, I just explained what it</p> <p>24 said.</p> <p>25 Q. Well, I'm sorry, maybe I missed</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. They all go into -- all those</p> <p>3 factors go into the agreed upon -- all the</p> <p>4 factors are agreed upon simultaneously and one</p> <p>5 will affect the other. So you may get a</p> <p>6 longer -- a longer lockup period and a higher</p> <p>7 discount or -- depending upon the preferences</p> <p>8 of the parties. Just something like that.</p> <p>9 Q. Now, you indicate that Badian's</p> <p>10 trading strategies and the way he unwound</p> <p>11 Amro's positions in Sedona's stock was</p> <p>12 consistent with a trading strategy that you</p> <p>13 refer to in paragraph 18.</p> <p>14 Now, what -- what was the trading</p> <p>15 strategy that you're referring to?</p> <p>16 MR. SOHN: Objection to the form.</p> <p>17 A. The trading strategy that's</p> <p>18 referred to in the previous sentence. To</p> <p>19 reduce -- "seek to reduce their overall long</p> <p>20 position in the underlying equity whenever</p> <p>21 possible and to" the extent -- "and to extend</p> <p>22 the period over which such positions were</p> <p>23 unwound."</p> <p>24 Q. Can -- are those -- those two</p> <p>25 statements consistent?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 it.</p> <p>3 You start as soon as possible.</p> <p>4 Reduce your overall long position in the</p> <p>5 underlying equity whenever possible. That</p> <p>6 means you start unwinding as soon as possible.</p> <p>7 Okay?</p> <p>8 Then it says "to extend the</p> <p>9 period over which such positions were</p> <p>10 unwound."</p> <p>11 What does that mean?</p> <p>12 A. No, I would say it differently. I</p> <p>13 would say whenever you see a chance -- whenever</p> <p>14 there is a chance, an optimal trading -- the</p> <p>15 first clause to me means whenever there is a</p> <p>16 chance to un -- to unwind your position, unwind</p> <p>17 your long position, you take it.</p> <p>18 And, furthermore, you -- and this</p> <p>19 is the second clause. You start that process</p> <p>20 as early as possible, because as soon as you</p> <p>21 invest in the FPS, you're at risk.</p> <p>22 Q. Well, if you have an FPS that</p> <p>23 is -- the price is a floating price based on</p> <p>24 stock price and you're buying at a discount --</p> <p>25 in this case I think it's 85 cents on the</p>

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<p>1 - STEPHEN D. PROWSE - 2 dollar. Right? 3 A. (Indicating.) 4 Q. What's the magnitude of the risk 5 when you're holding the -- holding the 6 debenture prior to conversion? 7 A. Well, that's where the nature of 8 the company comes in. The magnitude of the 9 risk is -- consists of a number of risks: 10 credit risk, default risk, liquidity risk, 11 delisting risk. And the size of those risks 12 depends on the riskiness of the company. 13 This was an extremely risky 14 company. Highly volatile stock price, very 15 poor operating performance, unable to raise 16 money in any other way than through an FPS. 17 Periods of time over which the stock price 18 could easily fall 90 percent. 19 This was a -- this was a company 20 that presented high credit risk, high default 21 risk, high liquidity risk and high delist -- 22 delisting risk. And all that together meant 23 that your holdings in the FPS were extremely 24 risky right from the get-go. 25 And, so, you would want to cover</p>	<p>1 - STEPHEN D. PROWSE - 2 Was that a rational economic 3 decision on their part? 4 MR. SOHN: Objection. It's an 5 incomplete hypothetical. 6 A. It may or may not have been. I 7 don't know if they were aware what they were -- 8 what they were entering into in terms of a 9 nonshort provision. It may or may not have 10 been an economically rational decision. 11 But once that decision's made and 12 you are in a position where you're in an FPS, 13 you're an extremely -- you're holding extremely 14 risky security. And a way to hedge that risk 15 is to short and cover yourself. 16 Q. Well, if it's a floating price 17 conversion, how great is the risk if the price 18 goes down? Don't you just get more stock 19 that's equal to the amount that you tendered 20 for the conversion? 21 A. That's one protection, but it's 22 not a complete protection. You've got -- as 23 I've said, as I said five minutes ago, you've 24 got credit risk, you've got default risk, you 25 have delisting risk, you have liquidity risk,</p>
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<p>1 - STEPHEN D. PROWSE - 2 yourself for that. 3 Q. Did Amro extend the convertible 4 debenture? 5 A. I believe it did. 6 Q. When did it do that? 7 A. I don't know the date. 8 Q. When did it begin to negotiate 9 that? 10 A. I don't know the date. 11 Q. Did Amro and Rhino and Badian sign 12 a nondisclosure agreement to look at the 13 financials of Sedona when they did so? 14 A. I'm not aware of whether they did 15 or didn't. 16 Q. So you don't know? 17 A. I don't know. 18 Q. Well, assume that they did, okay, 19 for purposes of giving your opinions. And they 20 decided to extend the term after they had seen 21 the financials on a confidential basis. And 22 they extended the debenture which had a 23 provision in it which prohibited them from 24 shorting the stock prior to submitting a 25 conversion letter.</p>	<p>1 - STEPHEN D. PROWSE - 2 all of which can result in a decline of the FPS 3 and a decline in the value of the FPS and a 4 decline in the value of the stock or your 5 ability to get cash out of the stock when you 6 eventually get it. 7 Q. Was all of that information 8 available to Badian and Rhino and Amro at the 9 time that they agreed to extend the convertible 10 debenture? 11 MR. SOHN: Objection to form. 12 A. I would assume that both Sedona 13 and Rhino are sophisticated parties. And when 14 they enter into a contract, they understand the 15 risks that they are entering into. And -- but 16 once you have entered into that contract, those 17 risks are there and you want to hedge them to 18 the -- to the greatest extent you can. 19 Q. Now, isn't -- isn't there a risk 20 in holding Sedona stock long? 21 MR. SOHN: When? 22 MR. GUIDO: At any point in time. 23 A. Sure, there's a risk with holding 24 any -- any kind of financial instrument. It's 25 just a question of whether it's a -- it's a</p>

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<p>1 - STEPHEN D. PROWSE - 2 question of the degree. 3 Q. The degree. Okay. 4 When Sedona converted -- I mean 5 when Amro converted the stock in their 6 conversions in the spring of 2001, did it end 7 up long, the stock? 8 A. It ended up long, the stock, but 9 not by much and for a short period of time. 10 Q. Well, what do you mean by "not by 11 much"? 12 A. Not by much. I mean, at most I 13 think a hundred -- a couple hundred thousand 14 shares, maybe, if that. 15 Q. Really? 16 A. For short periods. 17 Q. Really? 18 A. Yeah, really. 19 Q. Not 814,000? 20 A. Nowhere close to that. 21 Q. Nowhere close to that? 22 A. No. 23 Q. Where do you get that information? 24 A. From our database that you have. 25 Q. Well, you have the data -- you</p>	<p>1 - STEPHEN D. PROWSE - 2 quickly -- as soon as you can without having 3 any impact on the market. Slowly unwind your 4 long position till you get to a point at which 5 you can convert. Then make a decision about 6 whether you want to convert or not, depending 7 upon how much you've been able to cover 8 yourself. 9 And if you decide to convert, then 10 you have to decide how much you're going to 11 convert and that would depend on how much 12 you've been able to short. And then start 13 again depending on how much you have left to go 14 in terms of your conversion. 15 Q. Well, when did they -- when did 16 they start shorting the stock there? 17 A. You mean after November 22nd? 18 Q. Uh-huh. 19 A. I mean, I would have to look at 20 the data to tell you the day when they started, 21 but I can't tell you sitting here. 22 Q. Have you ever seen any of the 23 reports that Danny Graham sent to Andreas 24 Badian on the short transactions in the 25 Refco/Amro account?</p>
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<p>1 - STEPHEN D. PROWSE - 2 have the aggregate data, don't you, on that 3 Exhibit 14, or am I wrong in what's in Exhibit 4 14? No, I'm sorry, it's not in Exhibit 14. 5 But in your database it shows that 6 -- in the database it shows -- 7 A. Just the accumulated position in 8 terms of shares on a daily basis. 9 Q. On a daily basis. 10 And, so, that, after the 11 conversions, that Sedona was not long the stock 12 more than a few hundred thousand shares? 13 A. Well, I want to be careful about 14 the time period, but -- and there may have been 15 a brief period where it was a little more than 16 that, but I don't believe it was ever close to 17 being 860,000 shares long. 18 Q. Okay. So your view is that they 19 should short the stock as much as possible and 20 then they should convert and get rid of the 21 stock that they have as soon as possible? 22 A. I would phrase it differently. I 23 would phrase it that what they should do, or 24 what an optimal strategy would be for holding 25 an FPS, is to start hedging yourself as</p>	<p>1 - STEPHEN D. PROWSE - 2 A. No, I don't believe I have. 3 Q. I'd like you to take a look at a 4 document that's been previously marked as 5 Exhibit No. 57. And I'd like you to turn to 6 the page -- as you can see, this is an e-mail 7 on Wednesday, March 28th, from Danny Graham to 8 Andreas Badian. It's called a Refco 9 spreadsheet. 10 Look at the page SDNA, about the 11 third or fourth in. I guess it's not the third 12 or fourth. 13 Are you at that page? 14 A. Yes. 15 Q. This is a summary of the 16 transactions in the Refco account in Sedona -- 17 I mean in the Amro account. It's a -- I mean 18 the Refco account for Amro in Sedona stock. 19 And it indicates that the short selling 20 started, that's involved here, on February 21 21st. That is three months after the 22 convertible debenture was even entered, isn't 23 it? 24 A. Yes. 25 Q. Is that what you call as soon as</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 possible?</p> <p>3 A. Well, I don't know if this is the</p> <p>4 sum total of Rhino transactions. So, I just</p> <p>5 don't know whether this is representing all of</p> <p>6 Rhino's transactions.</p> <p>7 Q. So, Rhino or Amro could have been</p> <p>8 selling through other accounts other than the</p> <p>9 Refco account?</p> <p>10 A. They could have been.</p> <p>11 Q. Take a look at Exhibit No. 47</p> <p>12 again.</p> <p>13 Do you see that?</p> <p>14 MR. SOHN: Which one?</p> <p>15 MR. GUIDO: I think it was --</p> <p>16 MR. SCHECHTMAN: This one?</p> <p>17 MR. GUIDO: Excuse me. It was the</p> <p>18 21A report.</p> <p>19 THE WITNESS: This one?</p> <p>20 MR. GUIDO: What's the exhibit</p> <p>21 number?</p> <p>22 BY MR. GUIDO:</p> <p>23 Q. Does that reflect aggregate</p> <p>24 transactions in Sedona stock by Amro-related</p> <p>25 activities?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 to answer your question here.</p> <p>3 Q. Is it your understanding that</p> <p>4 Badian, acting on behalf of Amro, shorted the</p> <p>5 stock of Sedona prior to February 21st of</p> <p>6 2001?</p> <p>7 A. As I said before, I can't give you</p> <p>8 a date without looking at the data for the</p> <p>9 cumulative holdings which are in our -- in our</p> <p>10 work sheets. And the date just doesn't come to</p> <p>11 mind at which Rhino first was in a short</p> <p>12 position after issuance of the November 22nd</p> <p>13 FPS.</p> <p>14 Q. Now, assuming that you're correct,</p> <p>15 that that's what rational strategy in the</p> <p>16 shorts did occur at an earlier point in time,</p> <p>17 is it also an economically rational strategy to</p> <p>18 short the stock as much as possible, convert at</p> <p>19 a low price, and by pushing the price down</p> <p>20 using whatever market strength that Badian had,</p> <p>21 converting the larger number of shares and</p> <p>22 then, using NASDAQ trades to push up the market</p> <p>23 price and unload those additional shares at the</p> <p>24 higher price?</p> <p>25 MR. SOHN: Objection to form.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Does what --</p> <p>3 MR. SOHN: Objection to form.</p> <p>4 A. Does what reflect?</p> <p>5 Q. The Schedule D on Exhibit No. 10,</p> <p>6 which is the earlier Exhibit No. 47.</p> <p>7 MR. SOHN: Does it what?</p> <p>8 Q. It's Exhibit D, or Schedule D, on</p> <p>9 Exhibit No. 10.</p> <p>10 MR. SOHN: Right. And what's the</p> <p>11 question?</p> <p>12 Q. Does that reflect the aggregate</p> <p>13 transactions in Sedona stock during the time</p> <p>14 period after they were entering into the</p> <p>15 convertible debenture?</p> <p>16 MR. SOHN: Are you asking</p> <p>17 Dr. Prowse if that's accurate or if it reports</p> <p>18 what it purports to report?</p> <p>19 BY MR. GUIDO:</p> <p>20 Q. Does it purport?</p> <p>21 A. I don't even know what it</p> <p>22 purports. I haven't read this document. It's</p> <p>23 a very long document with 23 pages and a large</p> <p>24 number of spreadsheets. So I don't know what</p> <p>25 it's supposed to purport. So I don't know how</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, number one, that's a</p> <p>3 strategy that increases your risks in a number</p> <p>4 of aspects. And, number two, that's not what</p> <p>5 our empirical analysis finds, that there was no</p> <p>6 price impact one way or the other of Rhino's</p> <p>7 trades. And, so, with regards to number one,</p> <p>8 --</p> <p>9 Q. My --</p> <p>10 A. -- the optimal strategy --</p> <p>11 Q. Excuse me. I'm sorry for</p> <p>12 interrupting, but I'm not asking what they did</p> <p>13 here. I asked you a hypothetical.</p> <p>14 I said isn't it a rational</p> <p>15 strategy, economically rational, if you have</p> <p>16 the ability to do it -- to short stock at a</p> <p>17 higher price, push it down and convert at a</p> <p>18 lower price, and then to use mechanisms such as</p> <p>19 wash trades to push it up to give you the</p> <p>20 excess stock at a higher price? Isn't that an</p> <p>21 economically rational approach?</p> <p>22 MR. SOHN: Objection to form.</p> <p>23 A. I think a more economically</p> <p>24 rational approach is just to short the stock</p> <p>25 without any intent to push it down, cover</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 yourself. When you get to a point that you can</p> <p>3 convert, convert, and continue to do that all</p> <p>4 the way through to the end of the FPS. That</p> <p>5 avoids risks associated with manipulating the</p> <p>6 stock.</p> <p>7 Q. Well, let me give you a</p> <p>8 hypothetical. Okay? And that is the stock is</p> <p>9 trading at a buck. And, so, I short a million</p> <p>10 shares at a dollar. And I have the ability to</p> <p>11 push it down to 50 cents. And I push it down</p> <p>12 to 50 cents. And I convert at a 50-cent price.</p> <p>13 And I get my million shares -- I get the</p> <p>14 million shares that I sold at 50 cents and I</p> <p>15 get another million shares at 50 cents. And</p> <p>16 then I enter into wash sales and I push the</p> <p>17 price back up to a buck and I unload it.</p> <p>18 Don't I make much more money than</p> <p>19 I had sold -- than if I had sold the million</p> <p>20 shares and converted the million shares after,</p> <p>21 at a buck?</p> <p>22 A. I guess in your hypothetical, to</p> <p>23 the extent I understand it, you've set it up</p> <p>24 that way, yes. It's almost tautologic.</p> <p>25 Q. No, I understand that. But isn't</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 What's the question?</p> <p>3 MR. GUIDO: I'm sorry.</p> <p>4 MR. SCHECHTMAN: Wait. Ken, can</p> <p>5 we just get the question read back?</p> <p>6 MR. GUIDO: Yes.</p> <p>7 MR. SCHECHTMAN: Thank you.</p> <p>8 (Whereupon, the record is read</p> <p>9 back.)</p> <p>10 MR. GUIDO: Are we waiting for</p> <p>11 something?</p> <p>12 MR. SOHN: She didn't -- she</p> <p>13 didn't really have what the question was.</p> <p>14 MS. SCHECHTMAN: And it didn't</p> <p>15 sound like a question.</p> <p>16 MR. SOHN: It sounded even less</p> <p>17 like a question than it did the first time.</p> <p>18 MR. GUIDO: Let me ask you a</p> <p>19 question, or let me ask you the question with</p> <p>20 Ms. Schechtman's permission.</p> <p>21 BY MR. GUIDO:</p> <p>22 Q. And that is the -- are you telling</p> <p>23 me, or us, that there is no rational</p> <p>24 economic -- there's no economically rational</p> <p>25 reason to engage in market manipulation?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 it -- isn't that also a feasible strategy?</p> <p>3 A. I don't know if it's a feasible</p> <p>4 strategy or not. It depends on the stock, it</p> <p>5 depends on the entity, it depends on the risks</p> <p>6 of the security, it depends on the risks of the</p> <p>7 company. It depends on the risks of</p> <p>8 manipulating -- actually manipulating the</p> <p>9 stock, and depends on your ability to do that.</p> <p>10 Q. Well, there are a lot of</p> <p>11 uncertainties in life, including your -- your</p> <p>12 hypothetical of the appropriate hedging</p> <p>13 strategy, aren't there?</p> <p>14 MR. SOHN: Objection.</p> <p>15 A. That's not my hypothetical.</p> <p>16 That's my opinion.</p> <p>17 Q. Okay.</p> <p>18 A. It's your hypothetical of the --</p> <p>19 Q. It's my hypothetical. And your</p> <p>20 opinion is also a hypothetical. And that is</p> <p>21 that you basically short the stock and then you</p> <p>22 convert. Right?</p> <p>23 A. That's not a hypothetical.</p> <p>24 MR. SOHN: That's a question?</p> <p>25 MR. SCHECHTMAN: Wait. Stop.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. What I'm telling you is that,</p> <p>3 hypothetically, I can see that there would be</p> <p>4 economic incentives to engage in manipulation.</p> <p>5 Manipulation happens. It just doesn't happen</p> <p>6 in this case.</p> <p>7 There was a -- there was an</p> <p>8 economically rational strategy for trading the</p> <p>9 equity of Sedona based on the riskiness of the</p> <p>10 FPS, which was largely mirrored by Rhino's</p> <p>11 strategy, and there was no empirical evidence</p> <p>12 to support Rhino having -- having any impact on</p> <p>13 the price. And Sedona was a highly risky</p> <p>14 company whose stock price could go up, was</p> <p>15 extremely volatile. And that contributed to</p> <p>16 the optimality of the hedging strategy and also</p> <p>17 contributed to the riskiness of the stock and</p> <p>18 why it would go down.</p> <p>19 Q. Well, let me read you something.</p> <p>20 And that is, "Contract-based and trade-based</p> <p>21 manipulation is neither impossible nor</p> <p>22 self-detering. Possible economic models</p> <p>23 indicate that manipulation can be profitable."</p> <p>24 Manipulation -- "Manipulative trading may or</p> <p>25 may not be common, but it is possible and</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 tempting in a variety of significant and common</p> <p>3 situations."</p> <p>4 Do you agree or disagree with that</p> <p>5 statement?</p> <p>6 A. I think that's what I largely</p> <p>7 said, that there could be economic situations</p> <p>8 where manipulation works, but it just didn't</p> <p>9 work in this case. It didn't happen in this</p> <p>10 case for the reasons I just gave.</p> <p>11 Q. And you said it was based on</p> <p>12 empirical evidence?</p> <p>13 A. It's based on an analysis of the</p> <p>14 optimal trading strategy; it was based on an</p> <p>15 analysis of the risks Sedona presented to</p> <p>16 investors; and it was based on empirical</p> <p>17 analysis. Yes.</p> <p>18 Q. Was it based on what the people</p> <p>19 who were engaged in the activity themselves</p> <p>20 thought they were doing?</p> <p>21 MR. SOHN: Objection to form.</p> <p>22 A. It was based on the three inputs</p> <p>23 that I -- the three pieces of analysis that I</p> <p>24 talked about.</p> <p>25 Q. Okay. Did you consider at all</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. No.</p> <p>3 Q. The numbers, as far as you're</p> <p>4 concerned, are the controlling variable?</p> <p>5 A. No. My report is the -- my report</p> <p>6 is my report and all the elements of my</p> <p>7 report --</p> <p>8 Q. Okay.</p> <p>9 A. -- that go into that.</p> <p>10 Q. Okay. But I'm giving you another</p> <p>11 variable that you didn't consider.</p> <p>12 A. Correct.</p> <p>13 Q. And that is that the people who</p> <p>14 engaged in the activity concluded that they had</p> <p>15 pushed the price down to 75 cents at Badian's</p> <p>16 direction.</p> <p>17 MR. SOHN: Objection.</p> <p>18 Q. Does that affect your conclusions</p> <p>19 in your report?</p> <p>20 MR. SOHN: Objection to form.</p> <p>21 A. The evidence doesn't support that</p> <p>22 notion.</p> <p>23 Q. Well, let's go -- let's talk about</p> <p>24 the regressions now. You did five regressions</p> <p>25 on the March 1st to May 31st transactions. And</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 what the people who were executing the</p> <p>3 transactions thought they were doing?</p> <p>4 A. We didn't get -- we didn't get</p> <p>5 into that. We weren't asked to look at that.</p> <p>6 Q. So you've never seen or</p> <p>7 listened -- seen transcripts or -- of</p> <p>8 audiotapes or heard audiotapes of what</p> <p>9 Mr. Badian was saying or that people who were</p> <p>10 executing trades on his behalf were saying</p> <p>11 about what he was doing?</p> <p>12 A. I have not.</p> <p>13 Q. Would your opinion be affected if</p> <p>14 you learned that the people who had executed</p> <p>15 the trades had concluded that Badian had pushed</p> <p>16 the price down in order to increase his</p> <p>17 conversion, the number of shares to get on</p> <p>18 conversion?</p> <p>19 MR. SOHN: Objection to form.</p> <p>20 A. That's not what the data I've</p> <p>21 analyzed tells me. That's not what I've</p> <p>22 concluded in my report. So that wouldn't</p> <p>23 change my opinion.</p> <p>24 Q. So it wouldn't change your</p> <p>25 opinion?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 then there's another one that you don't list,</p> <p>3 and that is net daily trading excluding the</p> <p>4 impact to the NASDAQ, which you don't even</p> <p>5 mention.</p> <p>6 A. That's incorrect.</p> <p>7 Q. Well, I -- I don't see a piece of</p> <p>8 paper that says you did it. I had to have</p> <p>9 somebody go back and reconstruct the model to</p> <p>10 determine it. There's not a piece of paper</p> <p>11 that you've produced in this case that said you</p> <p>12 did that last regression.</p> <p>13 A. Which last regression?</p> <p>14 Q. The regression of net daily</p> <p>15 trading absent the impact of the NASDAQ. There</p> <p>16 is not a piece of paper that says you did that</p> <p>17 regression anywhere in what you've produced.</p> <p>18 A. Well, I understand -- I understand</p> <p>19 that we did that regression. I understand we</p> <p>20 did nine regressions, not five.</p> <p>21 Q. Okay.</p> <p>22 A. Nine regressions for each period.</p> <p>23 Q. Okay. Well, I'm sticking to the</p> <p>24 March 1st to May 31st -- March 1st to May 31st</p> <p>25 time period right now. Okay?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 And the -- the question is, you</p> <p>3 came up -- you did what you call nine</p> <p>4 regressions, and that three of them show a</p> <p>5 significant correlation, although one of them</p> <p>6 is weak. It's a 7.08, one which is net trading</p> <p>7 as a percentage of total volume.</p> <p>8 One of them is net daily trading</p> <p>9 factoring out the impact of the NASDAQ. And</p> <p>10 the third is net daily trading ignoring the</p> <p>11 impact of the NASDAQ, which you, in another</p> <p>12 correlation, have indicated during this time</p> <p>13 period is statistically insignificant in terms</p> <p>14 of its impact.</p> <p>15 So you've got three regressions</p> <p>16 that show a statistically significant</p> <p>17 relationship between Badian's trading activity</p> <p>18 and the stock price of Sedona.</p> <p>19 Now, why isn't that consistent</p> <p>20 with the testimony that I've just told you</p> <p>21 exists in this record that the people that</p> <p>22 engaged in the trading activity on behalf of</p> <p>23 Badian concluded that Badian had pushed the</p> <p>24 price down to 75 cents?</p> <p>25 MR. SOHN: Objection to form.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. And that is --</p> <p>3 MR. SOHN: Mr. Guido, please let</p> <p>4 the witness finish his answer.</p> <p>5 A. That is inconsistent with the --</p> <p>6 with the information you just gave me. And</p> <p>7 it's also consistent with your experts'</p> <p>8 analysis. Your experts ran our regressions for</p> <p>9 another time period, yet another time period.</p> <p>10 And in their time period, they found no -- even</p> <p>11 on a stand-alone basis no statistically</p> <p>12 significant -- a "P" value of less than 5</p> <p>13 percent.</p> <p>14 Q. All right. Let's talk about the</p> <p>15 massive evidence. Okay? One of them is</p> <p>16 NASDAQ. Right? The background. I'm taking --</p> <p>17 I'm using your report.</p> <p>18 A. Okay. I'm not sure what</p> <p>19 particular part of my report you're referring</p> <p>20 to.</p> <p>21 Q. Well, I mean, you're talking that</p> <p>22 you did a lot of analysis and there's a massive</p> <p>23 amount of amount. One of them is what NASDAQ</p> <p>24 did. The other is what the peer group did.</p> <p>25 The third is the events, the company-specific</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. For a variety of reasons. First</p> <p>3 off, none of the relationships that you've just</p> <p>4 described are properly considered to be</p> <p>5 significant when -- when considered in the</p> <p>6 context of the battery of tests we ran.</p> <p>7 We ran numerous parametric</p> <p>8 analysis, nonparametric analysis. We ran 18</p> <p>9 regressions. It doesn't surprise me at all</p> <p>10 that I would get a spurious correlation in two</p> <p>11 of them. It just doesn't. That's what --</p> <p>12 that's what to be expected from statistics.</p> <p>13 Controlling for that spurious</p> <p>14 correlation tells you that you cannot reject</p> <p>15 the hypothesis of no impact when you have a</p> <p>16 mass of results that tell you where the</p> <p>17 piece -- where the "P" value is greater than 5</p> <p>18 percent, and only two that tell you the "P"</p> <p>19 value is less than 5 percent.</p> <p>20 Q. Let's --</p> <p>21 A. So there is --</p> <p>22 MR. SOHN: Mr. Guido.</p> <p>23 A. There's a mass of evidence that</p> <p>24 shows no impact.</p> <p>25 Q. Okay. Mass of evidence --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 events.</p> <p>3 A. Actually I was talking about --</p> <p>4 Q. Anything else?</p> <p>5 A. -- the actual statistical</p> <p>6 analysis. But if -- but, certainly, that's</p> <p>7 true.</p> <p>8 Q. Okay.</p> <p>9 A. That's broadening out --</p> <p>10 Q. And you found that NASDAQ --</p> <p>11 (Indiscernible cross-talk; Reporter</p> <p>12 requests one speaker at a time.)</p> <p>13 A. Broadening it out to Section 3,</p> <p>14 yes, you're correct, those other factors also</p> <p>15 play a role.</p> <p>16 Q. Okay. And you testified that with</p> <p>17 NASDAQ, March -- March 1st to May 31st, there's</p> <p>18 no statistical correlation between the NASDAQ</p> <p>19 and Sedona's price. Correct?</p> <p>20 A. Correct, that's what the</p> <p>21 regression showed.</p> <p>22 Q. All right. And with regard to the</p> <p>23 peer group, you didn't do it, because you</p> <p>24 didn't have the data to do it. Right?</p> <p>25 A. I'm not sure if we didn't have the</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 data. I'm not sure that's the exact reason,</p> <p>3 but we didn't do it.</p> <p>4 Q. But you didn't do it.</p> <p>5 A. We didn't -- we didn't put it in</p> <p>6 the regressions. We looked at it and compared</p> <p>7 Sedona's stock price --</p> <p>8 Q. No, I understand. You didn't --</p> <p>9 A. -- decline --</p> <p>10 MR. SOHN: Mr. Guido.</p> <p>11 A. -- with the average decline of the</p> <p>12 peer group, found that it was totally in line.</p> <p>13 Q. You didn't do a statistical</p> <p>14 analysis comparing -- a regression analysis</p> <p>15 comparing the peer group performance with</p> <p>16 Sedona's stock performance, did you?</p> <p>17 A. We didn't do a regression</p> <p>18 analysis --</p> <p>19 Q. Thank you.</p> <p>20 A. -- with the peer index. We did</p> <p>21 another type of analysis.</p> <p>22 Q. Thank you.</p> <p>23 And you didn't do an event study</p> <p>24 on the various events that you cite in your</p> <p>25 report: The issuance of 10-Ks, the purchases</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Isn't that correct?</p> <p>3 A. That's exactly correct.</p> <p>4 Q. Okay.</p> <p>5 A. There was no impact of the -- of</p> <p>6 the trans -- of the transactions. And there</p> <p>7 was also no impact of the trades.</p> <p>8 Q. Now, so, then you've got -- you</p> <p>9 put those aside and you've got left the</p> <p>10 statistical analyses that you did on these</p> <p>11 three situations: One is that daily trades as</p> <p>12 a percentage of volume; net daily trades</p> <p>13 including factoring out the impact of NASDAQ;</p> <p>14 and, third, net daily trades of -- for not --</p> <p>15 not including the impact of the NASDAQ.</p> <p>16 Correct?</p> <p>17 A. As well as the other regressions</p> <p>18 we ran.</p> <p>19 Q. Okay. The other regressions.</p> <p>20 And the other regressions included</p> <p>21 regressions in which you put information that</p> <p>22 you have testified as far as you know was not</p> <p>23 public information?</p> <p>24 MR. SOHN: Objection.</p> <p>25 Q. Including transfers and -- and</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 of stock. You didn't do any event studies to</p> <p>3 indicate whether those in isolation had an</p> <p>4 impact on Sedona's stock price performance.</p> <p>5 A. That's incorrect, as we talked</p> <p>6 about a couple hours ago. And we went into</p> <p>7 that in detail a couple hours ago. That's just</p> <p>8 incorrect.</p> <p>9 Q. Where is the event study for each</p> <p>10 of those events? I didn't see it anywhere in</p> <p>11 your report.</p> <p>12 A. You mentioned an event study for</p> <p>13 stock purchases, and I -- we went through this</p> <p>14 two or three hours ago. I told you that we had</p> <p>15 indicator variables in our regressions for</p> <p>16 direct purchases of stock. And --</p> <p>17 Q. And when I looked at the -- when I</p> <p>18 looked at it, I think that the purchases of</p> <p>19 stock, you told me that you didn't see any</p> <p>20 significant correlation.</p> <p>21 A. Exactly. There was no impact on</p> <p>22 the price for Rhino's purchase of stock.</p> <p>23 Q. Okay. And there was no impact in</p> <p>24 terms of the transactions when you looked at</p> <p>25 those in isolation in your regression analyses.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 principal purchases.</p> <p>3 A. But potentially could have</p> <p>4 affected the price.</p> <p>5 Q. Okay.</p> <p>6 A. But reasonable --</p> <p>7 Q. You don't know --</p> <p>8 A. That's what were tested.</p> <p>9 Q. Okay. But you don't know?</p> <p>10 A. I don't know what?</p> <p>11 Q. I mean, isn't it a tautology?</p> <p>12 That's what we're testing? I mean, the</p> <p>13 question is, is the information public to have</p> <p>14 an impact? Don't have you to, you know, come</p> <p>15 to a conclusion of whether or not the</p> <p>16 information could possibly have had an impact?</p> <p>17 A. No, the question is, did Rhino's</p> <p>18 presence in the marketplace have an impact on</p> <p>19 the stock? Rhino was a large trader of this</p> <p>20 stock. It had potentially a very large supply</p> <p>21 of stock to sell into the market based on its</p> <p>22 FP -- because it was an FPS holder. Market</p> <p>23 participants would have understood that.</p> <p>24 Rhino's presence is absolutely -- in the</p> <p>25 marketplace is absolutely a potential factor in</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 determining the price because Rhino is an</p> <p>3 important trader in Sedona stock.</p> <p>4 Q. So, how can you conclude that it</p> <p>5 didn't have an impact on the price of the stock</p> <p>6 if what you just said was it was a major trader</p> <p>7 and everybody perceived it as being a major</p> <p>8 trader?</p> <p>9 A. Rhino was potentially a big trader</p> <p>10 in Sedona stock. So that's why you want to</p> <p>11 look at if, when it trades, it has an impact on</p> <p>12 the stock. We find it doesn't.</p> <p>13 Q. Well --</p> <p>14 A. So that's what -- that's what the</p> <p>15 data tell us. That's what we're testing.</p> <p>16 Q. Well, one of the data -- when you</p> <p>17 talk about magnitude in impact, one of the</p> <p>18 data's net daily trades. Right?</p> <p>19 A. One of the?</p> <p>20 Q. One of the regressions is net</p> <p>21 daily trades?</p> <p>22 A. One of the regressions has net</p> <p>23 daily trades in it.</p> <p>24 Q. Why isn't that significant in</p> <p>25 light of what you just said about, you know,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 entirely inappropriate. He's answering your</p> <p>3 question.</p> <p>4 MR. GUIDO: I think he keeps</p> <p>5 avoiding the question.</p> <p>6 BY MR. GUIDO:</p> <p>7 Q. My question is, okay -- I have a</p> <p>8 simple question for you. And it's just the</p> <p>9 same question I had for Mr. Beloreshki, and I</p> <p>10 believe he tried to avoid answering the</p> <p>11 question.</p> <p>12 And I want you to answer this</p> <p>13 question: Is if you take net daily trades,</p> <p>14 okay, and it shows a 95 percent significance of</p> <p>15 the impact of Badian's trading, what is the</p> <p>16 reason for rejecting that statistical analysis</p> <p>17 which you've done here and you didn't even</p> <p>18 include it because you say it was an oversight</p> <p>19 in your report?</p> <p>20 Explain to me why you exclude that</p> <p>21 without all of this other discussion about</p> <p>22 other things which you've testified are</p> <p>23 statistically not significant to the impact of</p> <p>24 Sedona stock. Just tell me with regard to that</p> <p>25 one regression analysis why you rejected it and</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Amro's market power in the marketplace?</p> <p>3 A. That's what the data tells you.</p> <p>4 That's what you want -- that's what you use the</p> <p>5 data to test. You have a theory.</p> <p>6 Q. Okay.</p> <p>7 A. And you want to test it. The</p> <p>8 theory is Rhino's presence in the marketplace</p> <p>9 potentially impacts the stock price. We want</p> <p>10 to test that. We did test that. We found that</p> <p>11 we could not -- we could not reject the null</p> <p>12 hypothesis of no impact.</p> <p>13 We did the same with Rhino's net</p> <p>14 daily trades, and the same with Rhino's net</p> <p>15 daily trades as a percentage of total volume.</p> <p>16 Q. Did you --</p> <p>17 A. Again, we couldn't reject the</p> <p>18 hypothesis.</p> <p>19 Q. Well, did --</p> <p>20 A. Hang on. I'm not finished.</p> <p>21 We couldn't reject the hypothesis</p> <p>22 of no impact.</p> <p>23 Q. I enjoy your filibustering, but I</p> <p>24 do have a limitation of time --</p> <p>25 MR. SOHN: Mr. Guido, that's</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 why you didn't include it in -- in your report</p> <p>3 and why you didn't explain why you excluded it</p> <p>4 from your report.</p> <p>5 MR. SOHN: Mr. Guido, the tone of</p> <p>6 your question is entirely inappropriate. The</p> <p>7 finger pointing is inappropriate. You're free</p> <p>8 to ask whatever questions, you know that, but</p> <p>9 there's an appropriate way to do it and an</p> <p>10 inappropriate way to do it.</p> <p>11 MR. GUIDO: I haven't said</p> <p>12 anything inappropriate.</p> <p>13 BY MR. GUIDO:</p> <p>14 Q. Would you please answer the</p> <p>15 question?</p> <p>16 A. First of all, you claimed that I</p> <p>17 didn't answer the question, and then you</p> <p>18 changed the question. We can go back and ask</p> <p>19 the court reporter what the question was that I</p> <p>20 was answering when you went off on me. And you</p> <p>21 will find that it's a different question than</p> <p>22 you just asked me.</p> <p>23 Q. Okay, let's --</p> <p>24 A. Secondly -- I'm not finished.</p> <p>25 Secondly, you asked me about four different</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 questions. So please ask me a question one at</p> <p>3 a time that I can answer.</p> <p>4 MR. GUIDO: Will the court</p> <p>5 reporter read back the question to the witness</p> <p>6 who doesn't seem to understand.</p> <p>7 MR. SOHN: Mr. Guido, I mean, the</p> <p>8 comments are inappropriate. Your question goes</p> <p>9 on for about four pages and -- and it's</p> <p>10 entirely reasonable that the witness is going</p> <p>11 to have a problem answering a four-page</p> <p>12 question.</p> <p>13 So if you could just ask a simple</p> <p>14 question, a straightforward question,</p> <p>15 Dr. Prowse is happy to answer it, as he's been</p> <p>16 doing all day.</p> <p>17 MR. GUIDO: All he has to say is</p> <p>18 "I don't understand the question" --</p> <p>19 MR. SOHN: Which is what he just</p> <p>20 said.</p> <p>21 MR. GUIDO: He didn't say</p> <p>22 that.</p> <p>23 A. I did say that. I said you asked</p> <p>24 me four questions and I don't know which one to</p> <p>25 answer. So ask -- ask me one and I'll answer</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 significant?</p> <p>3 A. Because after you adjust for the</p> <p>4 fact that you're making multiple tests, you</p> <p>5 have to adjust for the fact that multiple tests</p> <p>6 complicate the interpretation of a "P" value.</p> <p>7 This is a widely accepted scientific result.</p> <p>8 Q. What's the literature support --</p> <p>9 MR. SOHN: Mr. Guido.</p> <p>10 A. Now you interrupted me, so do you</p> <p>11 want me to now answer the next question?</p> <p>12 Q. Well, you just said you make an</p> <p>13 adjustment for multiple tests.</p> <p>14 A. You make an adjustment for</p> <p>15 multiple tests. And when you make that</p> <p>16 adjustment, it doesn't pass the Alpha</p> <p>17 threshold.</p> <p>18 Q. Okay. And what's the literature</p> <p>19 that supports that?</p> <p>20 A. There's a widely accepted</p> <p>21 literature. It's in many standard statistical</p> <p>22 text -- textbooks on multiple comparisons.</p> <p>23 David Kaye and David Freedman have talked about</p> <p>24 it in the Reference Guide on Statistics, which</p> <p>25 is part of the Reference Manual of Scientific</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 it.</p> <p>3 Q. Fine.</p> <p>4 MR. GUIDO: Can you read back the</p> <p>5 question?</p> <p>6 (Whereupon, the record is read</p> <p>7 back.)</p> <p>8 MR. SOHN: That's four questions.</p> <p>9 MR. GUIDO: That's five.</p> <p>10 A. I counted five.</p> <p>11 Q. Okay. One --</p> <p>12 MR. SOHN: We agree it's more than</p> <p>13 one.</p> <p>14 MS. SCHECHTMAN: We accept your</p> <p>15 apology, Mr. Guido.</p> <p>16 MR. SOHN: Do you have a question?</p> <p>17 BY MR. GUIDO:</p> <p>18 Q. Why did you regret -- reject</p> <p>19 Regression 5?</p> <p>20 A. What do you mean by "reject"? We</p> <p>21 didn't reject any regressions.</p> <p>22 Q. Well, you deemed that it wasn't</p> <p>23 significant, didn't you?</p> <p>24 A. It was -- it's not significant.</p> <p>25 Q. Okay. And why isn't it</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Evidence that is issued by the Federal Judicial</p> <p>3 Center, I believe; that multiple comparisons</p> <p>4 complicate the interpretation of a "P"</p> <p>5 statistic, of a probability statistic. And</p> <p>6 that if you run 20 different regressions, you</p> <p>7 shouldn't be surprised to find a spurious</p> <p>8 correlation even when the null hypothesis is</p> <p>9 true.</p> <p>10 Q. What edition of David Kaye's piece</p> <p>11 in the Reference Guide of Statistics are you</p> <p>12 referring to?</p> <p>13 A. I don't know.</p> <p>14 Q. When did you read that?</p> <p>15 A. I have a copy of it. I don't know</p> <p>16 what edition it is.</p> <p>17 Q. And you're -- you're saying that</p> <p>18 David Kaye supports your view when there are</p> <p>19 statistical -- that there are statistical</p> <p>20 methods for coping with multiple looks at the</p> <p>21 data.</p> <p>22 Is that a fair assessment?</p> <p>23 A. I don't remember reading that. I</p> <p>24 remember reading that multiple comparisons</p> <p>25 complicate the interpretation of a "P"</p>

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<p>1 - STEPHEN D. PROWSE - 2 statistic. And that if you do multiple tests, 3 you shouldn't be surprised to find a spurious 4 correlation when the null is true. 5 Q. Well, I have David Kaye in 2000, 6 and this is what David Kaye says in 2000. And 7 do you think this supports what you just said: 8 "There are statistical methods for coping with 9 multiple looks at the data which permit the 10 calculation of meaningful 'P' values in 11 certain cases." 12 Is that what you're referring to? 13 MR. SOHN: Mr. Guido, you're -- 14 first of all, I mean, you're asking the witness 15 about a document that you haven't shown him. 16 MR. GUIDO: Well, the -- 17 MR. SOHN: And you're -- and 18 you're pulling an excerpt out of it. So, I 19 mean, it's an unfair question. 20 MR. GUIDO: I'm making a 21 representation that that's a sentence that 22 appears in this -- in this piece. 23 BY MR. GUIDO: 24 Q. Is that what you're referring 25 to?</p>	<p>1 - STEPHEN D. PROWSE - 2 council. Okay? Take that example. 3 And, so, I decide that I'm going 4 to go out and do a survey of the residents of 5 lower Manhattan to get their view of whether or 6 not it should be rebuilt exactly the way it 7 existed before it came down. 8 And I go out and I do a survey. 9 You know, I apply all of the same appropriate 10 sampling methods and I come up with the answer 11 and I say, no, we don't want it rebuilt the way 12 it was. And I say, oh, boy. 13 So I commission another 14 statistical analysis, and they go out and they 15 come up with the same result. And, so, I end 16 up commissioning 20. So I come up with five of 17 the people that say, yes, I want it rebuilt. 18 Is what you're referring to -- and 19 I think your colleague referred to it as the 20 Bonferroni correction -- is that the situation 21 that is designed to apply to? 22 MR. SOHN: Objection to the form. 23 A. Well, I'm not sure I can reply to 24 your hypothetical. But the situation it's 25 supposed to apply to is when you have multiple</p>
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<p>1 - STEPHEN D. PROWSE - 2 A. I would have to see the context of 3 it. 4 Q. Why do you have to see the 5 context? Because you know -- 6 A. Because whenever -- because 7 whenever I'm quoted a sentence and asked what 8 it means, I like to see what the context is of 9 what's being talked about. 10 Q. Well, let me ask you this. I 11 mean, you -- you cited David Kaye. Anyone else 12 you want to cite? 13 A. There's a variety of articles out 14 there. Bonferroni, Dunn, Tukey. There's talk 15 about this in some -- in, I think, standard 16 statistical textbooks about multiple 17 comparisons. There's a variety of literature 18 out there on it. 19 Q. Well, let me ask you about the 20 literature. 21 Does the literature primarily 22 address this hypothetical, this situation? I 23 want to rebuild the World Trade Center just 24 exactly the way it was. So I -- and I want to 25 get support for that, to lobby the city</p>	<p>1 - STEPHEN D. PROWSE - 2 tests or multiple comparisons trying to find a 3 result and -- a universal result. 4 And the fact is that it's just -- 5 it's just the logic of statistics that if you 6 have -- the more regressions you run or the 7 more tests you do, the more likely you are to 8 find a spurious correlation. And you need to 9 control for that. 10 Q. The -- and what is the mathematics 11 that you do to control for that? 12 A. I think there are a variety of 13 different things you can do. There's the 14 Bonferroni correction; there's the Sidak 15 correction. They're very close, very similar. 16 There are -- 17 Q. Could you spell the second one? 18 A. S-i-d-a-k. 19 There are -- there are others that 20 are more subjective in terms of parsing the "P" 21 values across different tests, but the 22 Bonferroni correction is a very simple and 23 widely known correction to do. 24 Q. Have you read any of the 25 literature that's critical of the application</p>

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<p>1 - STEPHEN D. PROWSE - 2 of the Bonferroni correction? 3 A. I'm aware of some of it. 4 Q. And what does that literature say? 5 A. It generally says that, 6 particularly when you're doing extremely large 7 sampling, with very, very large number of 8 tests, that the Bonferroni correction can be 9 conservative. 10 Q. Have you ever read any literature 11 that indicates that the statistical methods for 12 coping with multiple looks of data would be of 13 little help in a case where analysts have run 14 through a variety of regression models to 15 arrive at the one considered the most 16 satisfactory? 17 MR. SOHN: You're asking if he's 18 ever read that sentence? 19 MR. GUIDO: No. 20 BY MR. GUIDO: 21 Q. Are you aware of literature that 22 indicates that that's a problem with using the 23 statistical approach? 24 A. I'm aware of literature -- the way 25 I interpret what you just said is what I've</p>	<p>1 - STEPHEN D. PROWSE - 2 drop a footnote in the report to that effect; 3 that this doesn't change my opinion because 4 this is a -- this is a spurious result as a 5 result of running a number of multiple tests 6 and because we need to control for that. 7 If you apply a Bonferroni 8 correction, it's -- this particular regression 9 still is not significant, as are -- as are none 10 of the -- as are all of the others not 11 significant. And, therefore, it doesn't -- 12 doesn't change my opinion. 13 I explained this morning that, 14 unfortunately, I forgot to drop that footnote 15 into the report before it issued. 16 Q. Well, isn't it -- isn't it 17 important for -- for an expert to include all 18 of the information that he bases his opinion on 19 in his report? 20 A. I don't often include all of the 21 analysis I do on a particular project in the 22 exhibits or in the text of my report. It 23 exists as a work sheet. It's a supporting work 24 sheet to either an exhibit or a piece of data 25 in the report.</p>
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<p>1 - STEPHEN D. PROWSE - 2 been saying for the past half an hour. And 3 that is that there's a -- there's a problem, 4 which is generally called data mining, which is 5 running multiple tests and then relying on one 6 in which you get a spurious correlation where 7 at -- where the result of the spurious 8 correlation is the fact -- simply the fact that 9 you've run multiple tests and the logic of 10 statistics tells you that you're getting hit a 11 spurious correlation for completely random 12 reasons even when the null is true. 13 Q. Well, did you actually do a 14 Bonferroni correction here? 15 A. I did. 16 Q. How come it's not in any of these 17 materials that were produced to me? 18 A. Well, the Bonferroni correction is 19 very easy to do. You -- all you do is adjust 20 the Alpha or the threshold "P" value by the 21 number of tests that you've run. 22 And when I -- when Erica reported 23 the "P" values to me, as I've discussed earlier 24 this morning, I noted that there was a "P" 25 value less than .05. And I reminded myself to</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. So you don't think it's relevant 3 to the jury to know that you did a regression 4 analysis that showed there was a statistical 5 correlation between Badian's trading activities 6 and Sedona's stock price? 7 MR. SOHN: Asked and -- asked and 8 answered. You just asked the same question. 9 A. And what -- what I just said is I 10 do think it's important to know. And that's 11 why I wanted to put a footnote into the report, 12 but, unfortunately, I forgot. But I'm telling 13 you now. 14 Q. Well, don't you have quality 15 control at FTI? 16 A. We do have quality control. 17 Unfortunately, you know, no one's perfect and 18 this was my fault because I was the one in 19 charge of the -- the last hurdle of this report 20 in terms of issuing it. And it was my fault 21 that that did not get into the report. 22 Q. Well, did you ever make an 23 attempt to evaluate whether or not each of the 24 models that were the basis for each of the 25 regressions were less strong than any of the</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 other models?</p> <p>3 MR. SOHN: Objection to the form.</p> <p>4 A. I think they're all legitimate.</p> <p>5 This is what Mr. Beloreshki and I discussed at</p> <p>6 the beginning. We want to try to understand</p> <p>7 all the potential ways that Sedona's stock</p> <p>8 price could be impacted by Rhino's trading and</p> <p>9 Rhino's transactions. We want to understand</p> <p>10 all the different ways that that could happen.</p> <p>11 And we understood going in that</p> <p>12 that would mean we might get a spurious result.</p> <p>13 But, you know, that's -- that's the problem</p> <p>14 with running multiple comparisons. Sometimes</p> <p>15 you will get a spurious result when you -- when</p> <p>16 you run a lot of them.</p> <p>17 Q. Well, why --</p> <p>18 A. But we wanted to cover all the</p> <p>19 bases.</p> <p>20 Q. I'm sorry. You did all of these</p> <p>21 regressions. Okay? And I think three of them</p> <p>22 include data that you don't even know whether</p> <p>23 or not -- was in the marketplace, could</p> <p>24 potentially affect the market. You're just</p> <p>25 surmising that.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 there's no impact on Sedona's stock from any</p> <p>3 measure of Rhino's trading.</p> <p>4 What we've got here is two</p> <p>5 spurious results out of very, very many. Two</p> <p>6 results where the "P" value is greater than --</p> <p>7 less than .05, out of very, very many results,</p> <p>8 both from the regression analysis and from the</p> <p>9 nonparametric and parametric analysis that tell</p> <p>10 us that there is no effect, including your own</p> <p>11 expert -- your own experts' specification of</p> <p>12 our Regression 5, which shows the same thing</p> <p>13 which -- over a different period which shows no</p> <p>14 statistically different effect.</p> <p>15 Q. Well, maybe, you know, I don't</p> <p>16 understand your vernacular.</p> <p>17 What do you mean by a "parametric</p> <p>18 test"?</p> <p>19 A. A parametric test is a test that</p> <p>20 assumes a distribution of the underlying stock</p> <p>21 returns in this particular case. Basically we</p> <p>22 assume a normal distribution in a parametric</p> <p>23 test.</p> <p>24 Q. And what's the normal distribution</p> <p>25 that you assumed here?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 MR. SOHN: Objection to form.</p> <p>3 MR. GUIDO: Let me finish.</p> <p>4 BY MR. GUIDO:</p> <p>5 Q. And you also indicated, I think</p> <p>6 you testified, that the magnitude of Badian's</p> <p>7 activity could be a relevant factor to</p> <p>8 consider.</p> <p>9 Why did you decide that the rules</p> <p>10 of finding correlation were spurious and not</p> <p>11 the others?</p> <p>12 A. Because there's a -- there's a</p> <p>13 potential to affect the stock price through any</p> <p>14 mechanism of a Rhino trade.</p> <p>15 Secondly, the results that we get</p> <p>16 have to be adjusted for the fact that you're</p> <p>17 going to get a spurious correlation. We just</p> <p>18 didn't -- we just didn't run nine regressions</p> <p>19 and rely on that. We wanted -- we wanted to</p> <p>20 rely on all the statistical analysis we did,</p> <p>21 including the nine regressions.</p> <p>22 And when you do that and you make</p> <p>23 a correction for the fact that you're testing</p> <p>24 this every which way, then you could -- then an</p> <p>25 appropriate conclusion, I believe, is that</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. It's normal. That it's normal.</p> <p>3 Q. The distribution to what?</p> <p>4 A. The distribution of stock returns</p> <p>5 over a period of time. The distribution, is it</p> <p>6 a bell-shaped curve or not?</p> <p>7 Q. And that that -- you knew</p> <p>8 eventually we were going to get to my little</p> <p>9 graph.</p> <p>10 MR. GUIDO: I'd like to have this</p> <p>11 marked as exhibit next number.</p> <p>12 (Whereupon, exhibit is received</p> <p>13 and marked BP-26 for identification.)</p> <p>14 BY MR. GUIDO:</p> <p>15 Q. I only hand you this because I</p> <p>16 wanted you to look at the little red graph</p> <p>17 there.</p> <p>18 Is that what you were referring to</p> <p>19 when you talk about normal distribution?</p> <p>20 A. A bell-shaped curve.</p> <p>21 Q. Okay. And is that an example of a</p> <p>22 bell-shaped curve, type curve?</p> <p>23 A. This is an example of a</p> <p>24 bell-shaped curve. The curve.</p> <p>25 Q. Okay. And one of the things that</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 you're doing with these statistical regressions</p> <p>3 is to decide where the data falls on that</p> <p>4 bell-shaped curve?</p> <p>5 A. Well, now we're back to</p> <p>6 regressions. I was talking about the</p> <p>7 parametric analysis.</p> <p>8 Q. Okay.</p> <p>9 A. But --</p> <p>10 Q. Excuse me.</p> <p>11 A. Okay. So if you want to go back</p> <p>12 to the regressions, that's fine.</p> <p>13 Q. No. Okay. How do you apply a</p> <p>14 parametric analysis to that?</p> <p>15 A. Well, a parametric analysis that</p> <p>16 we do in our report basically tests the</p> <p>17 difference between a particular distribution</p> <p>18 between the effect of Rhino's trade -- the</p> <p>19 affect of Rhino's buys versus sells on the</p> <p>20 stock price and whether the stock price -- and</p> <p>21 how much the stock price goes up or down based</p> <p>22 on the buys versus the sells versus the --</p> <p>23 versus the days when Rhino doesn't trade.</p> <p>24 Q. Okay.</p> <p>25 A. This is in -- summarized in</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 What about buys at the offer as</p> <p>3 opposed to no buys?</p> <p>4 A. Buys at the offer versus no buys?</p> <p>5 Q. Uh-huh.</p> <p>6 A. I would have to think about that.</p> <p>7 Q. Okay. Did you think about it when</p> <p>8 you prepared that exhibit?</p> <p>9 A. No, we thought this was the</p> <p>10 appropriate way to do it.</p> <p>11 Q. No, I understand that. But you</p> <p>12 didn't think about the alternatives, did you?</p> <p>13 A. No.</p> <p>14 MR. SOHN: He just answered the</p> <p>15 question.</p> <p>16 A. I just said we felt this was the</p> <p>17 appropriate way to conduct the parametric</p> <p>18 test.</p> <p>19 Q. And you just now said you'd have</p> <p>20 to think about the alternative I gave you.</p> <p>21 And my question is: Why didn't</p> <p>22 you think about that when you did this</p> <p>23 exhibit?</p> <p>24 A. Well, I'd have to think about the</p> <p>25 specific -- think about if that was a</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Exhibit -- in Exhibit 10, for example.</p> <p>3 Q. Okay. Let me ask you a question:</p> <p>4 Is there another way -- is there other ways --</p> <p>5 other data to analyze in that parametric test</p> <p>6 that was done here?</p> <p>7 MR. SOHN: Did other than what?</p> <p>8 Q. Other than buys and sells and no</p> <p>9 transactions.</p> <p>10 A. There could be. This is the way</p> <p>11 we did it. We felt this was the easiest way to</p> <p>12 do it, to group the -- to group the</p> <p>13 observations by buys and sells and nothing</p> <p>14 happening.</p> <p>15 Q. I just asked you whether there</p> <p>16 were other ways. I didn't ask you why you</p> <p>17 didn't do the other ways.</p> <p>18 A. Okay.</p> <p>19 Q. Let me ask my next question: What</p> <p>20 are the other ways? What are the other data</p> <p>21 points that you could include here?</p> <p>22 A. I mean, there's all sorts of ways</p> <p>23 you could group the data if you wanted to.</p> <p>24 Q. Well, let me give you an -- let me</p> <p>25 give you an example.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 reasonable way. We thought this was the</p> <p>3 reasonable way to do it.</p> <p>4 Q. Okay. Fine. Tell me what the</p> <p>5 other alternatives were that you thought</p> <p>6 about.</p> <p>7 A. I can't remember. There were -- I</p> <p>8 mean, you could group by -- could group by the</p> <p>9 extent to which the stock price moves versus a</p> <p>10 buy and a sell. You could group, you know --</p> <p>11 you could create a finer distinction instead of</p> <p>12 stock price moves between 0 and five, five and</p> <p>13 ten, ten and 15. Something like that.</p> <p>14 Q. Okay.</p> <p>15 A. You could create as big a matrix</p> <p>16 as you wanted in terms of buys and sells versus</p> <p>17 some characteristic of a stock price. You just</p> <p>18 have to be careful about the number of</p> <p>19 observations or the expected value you would</p> <p>20 get in each of those cells.</p> <p>21 Q. Well, could you -- could you do</p> <p>22 one of these -- what is it, Exhibit 10A? --</p> <p>23 using the percentage of volume, Sedona's</p> <p>24 percentage of volume or Badian's percentage of</p> <p>25 Sedona volume?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Rhino's percentage of Sedona</p> <p>3 volume. You might be able to do that.</p> <p>4 Q. Did you think about doing that?</p> <p>5 A. Well, we looked at that in our</p> <p>6 regression analysis, and we looked at that in</p> <p>7 our Exhibit 13, I believe -- 14 -- 12. Exhibit</p> <p>8 12. So that was covered in other exhibits.</p> <p>9 Q. In Exhibit 12. Okay. Let's look</p> <p>10 at Exhibit 12.</p> <p>11 And what did you conclude Exhibit</p> <p>12 12 demonstrated?</p> <p>13 A. That there was no significant</p> <p>14 relationship between trading volume and Sedona</p> <p>15 stock price returns.</p> <p>16 Q. Well, isn't this Exhibit 12 a</p> <p>17 graph of the Regression Number 5?</p> <p>18 A. No, it's not.</p> <p>19 Q. Well, it is a Regression Number 5</p> <p>20 for the larger time period, isn't it?</p> <p>21 A. No, it's not.</p> <p>22 Q. It's not?</p> <p>23 A. No.</p> <p>24 Q. This says this is a proportion of</p> <p>25 Rhino volume to market volume.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 you have -- and it's supposed to be an analysis</p> <p>3 of the proportion of Rhino volume to market</p> <p>4 volume, and then it has impacts on price</p> <p>5 returns. And that the -- a couple of questions</p> <p>6 I have about -- about this study.</p> <p>7 If you take a look at -- look</p> <p>8 between the 250 and the 300 percent range. You</p> <p>9 see that dot right above the black line?</p> <p>10 A. Yeah.</p> <p>11 Q. What is that?</p> <p>12 A. That's a -- that's a data point.</p> <p>13 Q. So what you're saying is that</p> <p>14 Rhino's trading volume was almost 300 percent</p> <p>15 of the total volume?</p> <p>16 A. On that particular day.</p> <p>17 Q. It was? How'd -- how'd that</p> <p>18 happen?</p> <p>19 A. Volume is measured here as buys</p> <p>20 plus sells. So, on that particular day, buys</p> <p>21 plus sells would have -- may have -- would have</p> <p>22 been greater than 300 percent. I think there's</p> <p>23 one day, actually -- I don't know if it's this</p> <p>24 day. I think there's one day in our database</p> <p>25 where we observed Rhino volume being greater</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Right.</p> <p>3 Q. And isn't that -- Rhino's --</p> <p>4 Sedona trades as a percentage of the total</p> <p>5 volume?</p> <p>6 A. No.</p> <p>7 Q. Well, did you do this for the</p> <p>8 shorter period of time?</p> <p>9 A. Did we do Exhibit 12 for the</p> <p>10 shorter period of time? I don't believe we</p> <p>11 did. We may have. If we did, it's in the work</p> <p>12 sheets.</p> <p>13 Q. Pardon?</p> <p>14 A. If we did, it's in the work</p> <p>15 sheets, but I don't believe we did.</p> <p>16 Q. Well, I mean, just take Exhibit</p> <p>17 No. 12. I mean, this, to me, is a scattergram.</p> <p>18 I don't know if that's an appropriate term.</p> <p>19 But it looks I can a scattergram. You have all</p> <p>20 these points --</p> <p>21 A. You could call it that.</p> <p>22 Q. Huh?</p> <p>23 A. You could call it that.</p> <p>24 Q. You have all of these points that</p> <p>25 are all over this scattergram. Okay? And that</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 than the market volume. And we're not sure of</p> <p>3 the reason why.</p> <p>4 Q. Well, I mean, how can that be?</p> <p>5 A. Well --</p> <p>6 Q. I mean, my understanding --</p> <p>7 A. Well, if the statements -- if the</p> <p>8 statements say a transaction occurred on this</p> <p>9 day, we have volume at a particular amount, we</p> <p>10 can't reconcile that. So that is one data</p> <p>11 point that may be -- may be problematic. But I</p> <p>12 don't know if it's this one.</p> <p>13 Q. Well, what is your understanding</p> <p>14 of how the total volume reported on Bloomberg</p> <p>15 is calculated?</p> <p>16 A. For the NASDAQ, both sides of the</p> <p>17 transaction are reported.</p> <p>18 Q. As one transaction.</p> <p>19 A. So you may -- so you get some</p> <p>20 double counting as you go through. You may</p> <p>21 get --</p> <p>22 Q. What?</p> <p>23 A. You may get some double counting</p> <p>24 as you go through.</p> <p>25 Q. Really?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. You may do.</p> <p>3 Q. You may?</p> <p>4 A. Yeah.</p> <p>5 Q. So the buys are reported to the</p> <p>6 market?</p> <p>7 A. So volume may be -- may be double</p> <p>8 what it's supposed to be.</p> <p>9 Q. Have you ever studied the audit</p> <p>10 trail reports on how the Bloomberg is developed</p> <p>11 off of the audit trail reports?</p> <p>12 A. No, I have not.</p> <p>13 Q. You have no idea how the Bloomberg</p> <p>14 data gets reported?</p> <p>15 A. I'd have to look and see.</p> <p>16 Q. But you can't tell us today?</p> <p>17 A. I can't tell you sitting here</p> <p>18 today.</p> <p>19 Q. Did you ever know?</p> <p>20 A. Yeah, I think I've known. I think</p> <p>21 I've known.</p> <p>22 Q. Did you ever -- did you ever do</p> <p>23 any research on that question?</p> <p>24 A. I've read articles on that.</p> <p>25 Q. On the question?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 time?</p> <p>3 A. We did nine --</p> <p>4 MR. SOHN: Objection to the form.</p> <p>5 I think there are least three false</p> <p>6 assumptions in there and three or four</p> <p>7 questions in there.</p> <p>8 A. That's correct, there are. But in</p> <p>9 answer to your final question, we did nine in</p> <p>10 the long period and nine in the shorter</p> <p>11 period.</p> <p>12 Q. Okay. Fine.</p> <p>13 And is the reason you rejected the</p> <p>14 findings of statistical significance in the</p> <p>15 three, in the shorter period of time -- one of</p> <p>16 which I think the literature we characterized</p> <p>17 as weak, that being the daily trading as a</p> <p>18 percentage of volume because it isn't at the 95</p> <p>19 percent significance level. The reason you</p> <p>20 rejected those three is because you came up</p> <p>21 with 15 others that showed no statistical</p> <p>22 significance?</p> <p>23 MR. SOHN: Objection;</p> <p>24 mischaracterizes the previous testimony.</p> <p>25 A. Right, it does. We didn't reject</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Yeah.</p> <p>3 Q. Have you ever read any of the</p> <p>4 NASDAQ guidance on riskless principal</p> <p>5 transactions?</p> <p>6 A. No, I have not.</p> <p>7 Q. No?</p> <p>8 Well, you didn't do the</p> <p>9 scattergram for the shorter period of time?</p> <p>10 A. I'm saying I can't remember if we</p> <p>11 did it. If we did it, it's in the work sheets.</p> <p>12 If it's not in the work sheets, we didn't do</p> <p>13 it.</p> <p>14 Q. Now, I'm still a little puzzled by</p> <p>15 what it is that you did that led you to</p> <p>16 conclude that the three analyses that showed</p> <p>17 correlation -- or significant -- excuse me. I</p> <p>18 you used the "C" word and I'm sorry, Mr. Sohn</p> <p>19 and Mr. Glosten.</p> <p>20 That you rejected the three in the</p> <p>21 shorter period of time. And your reason for</p> <p>22 doing that is because, in the longer period of</p> <p>23 time, you didn't show any statistical</p> <p>24 significance for -- was it nine regressions you</p> <p>25 said that you did for the longer period of</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 any regression. We considered all the</p> <p>3 regressions. We set up the design of the study</p> <p>4 to investigate the -- all the potential routes</p> <p>5 that Rhino's trades could impact Sedona's stock</p> <p>6 price.</p> <p>7 After running all the regressions,</p> <p>8 all 18 of them, we found that there was a "P"</p> <p>9 value greater than .05 in two of them. Those</p> <p>10 are spurious correlations, and you can't use</p> <p>11 them to deduce an impact on a stock price when</p> <p>12 you've got numerous other results that tell you</p> <p>13 that there's no impact.</p> <p>14 Q. Well, why are those spurious? And</p> <p>15 why -- why not the others be spurious?</p> <p>16 A. The others aren't spurious -- the</p> <p>17 others -- the others failed to reject the --</p> <p>18 failed to -- failed to reject the null on their</p> <p>19 face. They have "P" values that are sometimes</p> <p>20 very high.</p> <p>21 It's a generally accepted</p> <p>22 principle that when you run multiple tests and</p> <p>23 you get -- you should expect to get -- just by</p> <p>24 the nature of statistics, you should expect to</p> <p>25 get a spurious correlation now and again. And</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 if you properly adjust for that, you get --</p> <p>3 what you get from the entire battery of tests</p> <p>4 is the fact that there's the conclusion that</p> <p>5 there's no impact.</p> <p>6 Q. So --</p> <p>7 A. And, again, I would say that's</p> <p>8 confirmed by your own experts who ran the</p> <p>9 Number 5 regression on a shorter period of time</p> <p>10 than we did and found -- and found on its face</p> <p>11 a "P" value greater than .05, greater than 5</p> <p>12 percent. That just shows you how spurious this</p> <p>13 correlation is.</p> <p>14 Q. So you're saying that Professors</p> <p>15 Glosten and Jones ran the regression of the net</p> <p>16 daily trades for a shorter period of time and</p> <p>17 found that their hypothesis couldn't -- that</p> <p>18 their analysis could not be checked? The null</p> <p>19 hypothesis.</p> <p>20 A. Correct. It's in their work</p> <p>21 sheets.</p> <p>22 Q. It's in their work sheets? Which</p> <p>23 work sheet?</p> <p>24 A. Well, I don't know.</p> <p>25 Q. Well, I mean, you're the one who's</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. -- that you said that they</p> <p>3 prepared. And that it reject -- it failed to</p> <p>4 reject the null hypothesis?</p> <p>5 A. That's my understanding, yeah.</p> <p>6 But --</p> <p>7 Q. What were the -- and it was net</p> <p>8 daily trades?</p> <p>9 A. I believe -- that's my</p> <p>10 understanding. I believe so.</p> <p>11 Q. Now -- so, based on that result</p> <p>12 and the fact that you came up with 15 other</p> <p>13 results, you rejected the three analyses that</p> <p>14 found a statistically significant relationship</p> <p>15 between Badian's trading activity and Sedona's</p> <p>16 stock price?</p> <p>17 MR. SOHN: Objection;</p> <p>18 mischaracterizes the testimony again.</p> <p>19 A. Yeah, you have mischaracterized my</p> <p>20 testimony. We did not, for the third or fourth</p> <p>21 time, we did not reject any regressions. We</p> <p>22 considered all the regressions as a family</p> <p>23 based on the fact -- and based on the fact that</p> <p>24 the "P" values for most of our regressions --</p> <p>25 and, by the way, all our nonregression</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 making the allegation and I just want to know</p> <p>3 what you're talking about.</p> <p>4 A. Well, I told you what I know. And</p> <p>5 I can't identify the particular page, but --</p> <p>6 Q. Is it in --</p> <p>7 A. -- if I'm right, I'm right; and if</p> <p>8 I'm wrong, I'm wrong.</p> <p>9 Q. Is it in their report?</p> <p>10 A. No.</p> <p>11 Q. Oh, it's not in their report?</p> <p>12 A. No.</p> <p>13 Q. Where is it?</p> <p>14 A. It's in the work sheets that they</p> <p>15 produced.</p> <p>16 Q. And it's -- it's in the work</p> <p>17 sheets that they produced to whom?</p> <p>18 A. To us.</p> <p>19 Q. And in those work sheets, you said</p> <p>20 it was a shorter period of time?</p> <p>21 A. I believe it was through -- I</p> <p>22 think it was the month of March.</p> <p>23 Q. So it was March 1st through March</p> <p>24 30th was the regression --</p> <p>25 A. Maybe, yeah.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 statistical analysis -- is greater than .05.</p> <p>3 The "P" values that are greater</p> <p>4 than .05 are clearly spurious correlations.</p> <p>5 And when you do multiple comparisons, you need</p> <p>6 to adjust for that danger. When you run --</p> <p>7 when you run an extra regression, you increase</p> <p>8 the chance of finding a statistically -- or a</p> <p>9 "P" value of greater than .05.</p> <p>10 Q. And --</p> <p>11 A. Less -- less than .05.</p> <p>12 Q. And doesn't the literature suggest</p> <p>13 that to determine which of those are the</p> <p>14 regressions that should be relied upon for your</p> <p>15 conclusions that you look to how the model has</p> <p>16 been developed?</p> <p>17 A. Well, presumably the models that</p> <p>18 you are developing hypothetically -- in your</p> <p>19 hypothetical are all appropriate models for</p> <p>20 looking at the impact or whatever relationships</p> <p>21 you're trying to find.</p> <p>22 Q. Well, aren't some models more</p> <p>23 powerful than others?</p> <p>24 A. Some may be.</p> <p>25 Q. Well, what does the concept of</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 power mean when you're talking about comparing</p> <p>3 different regressions? Not the results of the</p> <p>4 regressions, but power when you're trying to</p> <p>5 decide whether the Regression 1, 2, 3, 4, 5, 6</p> <p>6 are more or less powerful than any of the</p> <p>7 others?</p> <p>8 A. Well, that doesn't have to do with</p> <p>9 the economic theory behind the variables. It</p> <p>10 has to do with the ability of the regression to</p> <p>11 find a relationship or not.</p> <p>12 MR. SOHN: May I make a</p> <p>13 suggestion? Just because I know they lock the</p> <p>14 door at six and it's ten to six right now. So</p> <p>15 maybe now's a good time for five minutes.</p> <p>16 MR. GUIDO: We'll take a break.</p> <p>17 THE VIDEOGRAPHER: This concludes</p> <p>18 Tape Number 4 in the videotaped deposition of</p> <p>19 Dr. Stephen Prowse. Going off the record at</p> <p>20 5:52 p.m.</p> <p>21 (A recess is taken.)</p> <p>22 THE VIDEOGRAPHER: This begins</p> <p>23 Tape Number 5 in the videotaped deposition of</p> <p>24 Dr. Stephen Prowse. Going back on the record</p> <p>25 at 6:05 p.m.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 towards finding -- towards -- I don't believe</p> <p>3 he had any biases, as neither do I. We</p> <p>4 discussed the appropriate regression models to</p> <p>5 run in this matter. We agreed on them and we</p> <p>6 ran them.</p> <p>7 Q. Well, did you read The Frontiers</p> <p>8 of Convertible Financing that he wrote with</p> <p>9 Caryn Schechtman?</p> <p>10 A. Yes.</p> <p>11 Q. Did that indicate to you that he</p> <p>12 had any biases?</p> <p>13 A. No, that didn't indicate to me he</p> <p>14 had any bias. I regard him as a very, very</p> <p>15 accomplished economist and statistician who has</p> <p>16 a former trading background. And I value his</p> <p>17 opinion very highly and I think he's a very --</p> <p>18 he has a very high level of integrity in terms</p> <p>19 of running empirical analyses.</p> <p>20 Q. Okay. Is the existence of a bias</p> <p>21 by an expert something that the jury should be</p> <p>22 concerned about?</p> <p>23 MR. SOHN: Objection.</p> <p>24 A. Well, I don't know what you mean</p> <p>25 by bias. I know I'm not biased. I know</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 BY MR. GUIDO:</p> <p>3 Q. Now, Mr. Prowse, when -- when you</p> <p>4 first came into working on the Sedona matter,</p> <p>5 in all of the -- had the 18 regression analyses</p> <p>6 been done?</p> <p>7 A. I don't know what had been done</p> <p>8 prior to me getting involved. I know some of</p> <p>9 the -- some or all of the nine specifications</p> <p>10 or the nine regression models that</p> <p>11 Mr. Beloreshki and I decided were appropriate</p> <p>12 to run in this matter had been run previously,</p> <p>13 but I don't know over what time periods those</p> <p>14 regressions --</p> <p>15 Q. Do you know --</p> <p>16 A. -- had been run.</p> <p>17 Q. -- who selected those?</p> <p>18 A. I believe it was Mr. Beloreshki.</p> <p>19 Q. Okay. Did you ever attempt to</p> <p>20 determine whether or not he had any biases?</p> <p>21 A. I don't know what you mean by</p> <p>22 whether he had any biases.</p> <p>23 Q. A bias towards -- towards finding</p> <p>24 a null hypothesis.</p> <p>25 A. I don't believe he had a bias</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Mr. Beloreshki isn't biased in any manner.</p> <p>3 We're economists. We perform economic and</p> <p>4 financial analysis, and we are guided by</p> <p>5 what that economic and financial analysis</p> <p>6 tells us.</p> <p>7 Q. Okay. What percentage of your</p> <p>8 income in the last five years has come from</p> <p>9 activities other than fees for testifying as an</p> <p>10 expert witness?</p> <p>11 MR. SOHN: Objection to the form.</p> <p>12 A. That's a question I can't answer</p> <p>13 because I don't get paid on the basis of fees</p> <p>14 that I generate for expert witness work versus</p> <p>15 other work that I do. I get paid a salary by</p> <p>16 FTI for performing a variety of different</p> <p>17 economic and financial analyses, some of which</p> <p>18 are involved in litigation or disputes; some of</p> <p>19 which is not.</p> <p>20 Q. Okay. Well, what percentage is</p> <p>21 involved in litigation or disputes of the work</p> <p>22 that you've done over the last five years?</p> <p>23 A. Over the last five years, I would</p> <p>24 say -- I don't know what time period you're</p> <p>25 talking about within those five years, but on</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 average I would say maybe about 50 percent is</p> <p>3 litigation or dispute related. There may or</p> <p>4 may not be a litigation. There may be a</p> <p>5 potential dispute between two parties, and I'm</p> <p>6 hired before litigation to maybe find an answer</p> <p>7 that might be acceptable to both parties, but</p> <p>8 there's the potential for a lawsuit there.</p> <p>9 Q. What about in the last two</p> <p>10 years?</p> <p>11 A. I would say probably the same. I</p> <p>12 don't really -- I don't really track how much</p> <p>13 of my time is on one type of project versus</p> <p>14 another type of project.</p> <p>15 Q. How important is the timeliness</p> <p>16 of the disclosure of the material that you</p> <p>17 relied upon to the credibility of an expert</p> <p>18 witness?</p> <p>19 A. I don't understand the question.</p> <p>20 Q. Well, you testified in how many</p> <p>21 matters?</p> <p>22 A. At trial?</p> <p>23 Q. Uh-huh.</p> <p>24 A. I don't know. A dozen, maybe a</p> <p>25 little more than a dozen.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, there was a disk that was</p> <p>3 provided to the SEC last night.</p> <p>4 Do you know that?</p> <p>5 A. Yes, I believe I do know it.</p> <p>6 Q. Okay. And you participated in</p> <p>7 preparing that disk. Correct?</p> <p>8 A. I instructed that certain files be</p> <p>9 put on that disk, right.</p> <p>10 Q. How many files were put on that</p> <p>11 disk?</p> <p>12 A. I don't know the total because I</p> <p>13 was only a part of the production. But I know</p> <p>14 that my production -- I understand that my</p> <p>15 production was from the Pet Quarters file,</p> <p>16 basically, that you requested and that we</p> <p>17 produced.</p> <p>18 And I'll tell you right now that</p> <p>19 99 percent of what I produced is completely</p> <p>20 irrelevant to what -- to the issues in this</p> <p>21 matter, because it has to do with our response</p> <p>22 to a Pet Quarters expert who basically did a</p> <p>23 valuation analysis or a damages analysis. But</p> <p>24 we decided to give it to you because we didn't</p> <p>25 want to -- even though it was completely</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. And have you ever had a situation</p> <p>3 where you produced documents the night before</p> <p>4 your deposition?</p> <p>5 A. Yes.</p> <p>6 Q. You have?</p> <p>7 A. Uh-huh.</p> <p>8 Q. Did the opposing party object to</p> <p>9 that?</p> <p>10 A. I can't remember them objecting,</p> <p>11 no.</p> <p>12 Q. How often has that happened?</p> <p>13 A. More than once.</p> <p>14 Q. How voluminous was the material</p> <p>15 that was produced the night before?</p> <p>16 A. I can't tell you.</p> <p>17 Q. Do you know how voluminous the</p> <p>18 material was that was produced to the SEC last</p> <p>19 night at 8:07?</p> <p>20 A. Are you referring to the GOJO</p> <p>21 documents or the RA documents or something</p> <p>22 else?</p> <p>23 Q. The disk.</p> <p>24 A. What do you mean by "the disk"? I</p> <p>25 don't know what you mean by "the disk."</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 irrelevant, we didn't want to -- we just wanted</p> <p>3 to give it to you.</p> <p>4 Q. Did the magistrate think it was</p> <p>5 irrelevant?</p> <p>6 A. Did the who?</p> <p>7 Q. The magistrate.</p> <p>8 A. Well, I don't know what the</p> <p>9 magistrate decided, but we were asked to</p> <p>10 produce our Pet Quarters file. And even though</p> <p>11 I knew it was going to be completely</p> <p>12 irrelevant, I said fine. So I can guarantee</p> <p>13 you that 99 percent of what I produced on there</p> <p>14 you needn't waste any time on because it</p> <p>15 doesn't address --</p> <p>16 Q. Do you know how many files were</p> <p>17 included?</p> <p>18 A. From what --</p> <p>19 MR. SOHN: Asked and answered.</p> <p>20 A. From what I produced?</p> <p>21 Q. Yeah.</p> <p>22 A. I can't tell you the number of</p> <p>23 files. I know we did a lot of work on Pet</p> <p>24 Quarters on the valuation or damages piece, so</p> <p>25 I expect there were a lot of files. But I can</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 tell you now you can save time by not going</p> <p>3 through them because you won't find them of</p> <p>4 interest. At least I don't believe you'll find</p> <p>5 them of interest unless you're interested in</p> <p>6 valuation and damages analyses.</p> <p>7 Q. Do you know -- do you know how</p> <p>8 large in terms of gigabytes the files were that</p> <p>9 were produced last night?</p> <p>10 A. I can't tell you how large they</p> <p>11 are. I can just tell you what I produced in</p> <p>12 terms of substance, content.</p> <p>13 Q. Do you have a -- is there a limit</p> <p>14 on your -- do you have an Outlook file?</p> <p>15 A. Do I have an -- you mean an</p> <p>16 e-mail?</p> <p>17 Q. An e-mail Outlook file.</p> <p>18 A. Yeah.</p> <p>19 Q. And you allow -- are you allocated</p> <p>20 a certain size on the server for that Outlook</p> <p>21 file?</p> <p>22 A. For my e-mail file?</p> <p>23 Q. Uh-huh.</p> <p>24 A. I presume -- I presume so. I</p> <p>25 don't know.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 those files which you say are totally</p> <p>3 irrelevant, on a disk with over eight hundred</p> <p>4 files, would that have made it difficult for me</p> <p>5 to find the files to question you today?</p> <p>6 MR. SOHN: Objection to the</p> <p>7 suggestion in the question.</p> <p>8 A. I can't -- I can't speak to that</p> <p>9 question. I don't know exactly how many files</p> <p>10 were part -- were my production with regards to</p> <p>11 the valuation/damages analysis of Pet Quarters.</p> <p>12 I'm not -- I don't know how quick you are with</p> <p>13 your computer.</p> <p>14 Q. Well, no matter how proficient I</p> <p>15 am with a computer, do you think that anyone</p> <p>16 could have gone through two gigabytes of</p> <p>17 documents to prepare for your deposition today</p> <p>18 if they received them at eight o'clock last</p> <p>19 night?</p> <p>20 MR. SOHN: Objection.</p> <p>21 A. I'm -- I can't answer that</p> <p>22 question. Sorry.</p> <p>23 Q. Well, you've worked with data,</p> <p>24 haven't you?</p> <p>25 A. Yeah.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Do people at FTI have certain</p> <p>3 space, size limitations, on what they can put</p> <p>4 on the servers at FTI?</p> <p>5 A. I just don't know the answer to</p> <p>6 that.</p> <p>7 Q. Would it surprise you that the</p> <p>8 disk that was produced to us last night had</p> <p>9 over eight hundred files on it?</p> <p>10 A. I can't speak to what was put on</p> <p>11 there apart from what I put on there. I know</p> <p>12 we did a lot of work on the valuation and</p> <p>13 damages aspect of the Pet Quarters matter. And</p> <p>14 you're free to look at it, but I can tell you</p> <p>15 now you probably don't want to waste too much</p> <p>16 time on it.</p> <p>17 Q. Well, would the existence of all</p> <p>18 of those files on that disk last night have</p> <p>19 made it impossible for me to go through the</p> <p>20 files to find files that are relevant to ask</p> <p>21 you questions today?</p> <p>22 A. Was that a question?</p> <p>23 Q. Yeah.</p> <p>24 A. What is the question?</p> <p>25 Q. Well, is the existence of all of</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. I mean, you have a sense of how</p> <p>3 quickly you can go through files, don't you?</p> <p>4 A. Yeah. And if you -- I don't know</p> <p>5 how the files were organized and I don't know</p> <p>6 what the titles of them were on. But if you</p> <p>7 had read the Pet Quarters report closely, which</p> <p>8 was produced weeks ago, you would know that we</p> <p>9 had a substantial amount of analysis that was</p> <p>10 devoted to rebutting a plaintiff's expert</p> <p>11 called Mr. Trugman, who did a valuation and</p> <p>12 damages analysis.</p> <p>13 And to the extent that you can</p> <p>14 identify quickly files on that disk that relate</p> <p>15 to Trugman and valuation and damages, I would</p> <p>16 think, clearly, that you wouldn't want to spend</p> <p>17 any time with them.</p> <p>18 Q. Well, taking the files that you</p> <p>19 produced, how were they described?</p> <p>20 A. I can't tell you. I don't know</p> <p>21 how they were organized. There was probably</p> <p>22 some logic to them and there was probably</p> <p>23 some -- there was probably some names that --</p> <p>24 that I would recognize in terms of the types of</p> <p>25 analysis that went into the Trugman analysis</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 and that you may have read if you were familiar</p> <p>3 with the analysis we did in Pet Quarters with</p> <p>4 regards to the valuation analysis.</p> <p>5 Q. I looked at this disk and I spent</p> <p>6 a fair amount of time looking at this disk, and</p> <p>7 there are no files in here that have a</p> <p>8 description on the file, when I open up the</p> <p>9 disk, that say that this is the damages</p> <p>10 analysis from Pet Quarters.</p> <p>11 Did you -- when you provided the</p> <p>12 disk, did you provide a description with them</p> <p>13 so that they could be easily reviewed to</p> <p>14 determine which ones were relevant for your</p> <p>15 testimony today?</p> <p>16 MR. SOHN: Objection.</p> <p>17 A. I just asked for the files to be</p> <p>18 produced. I would assume they would just be</p> <p>19 produced as they existed on our server.</p> <p>20 Q. And didn't the files exist on your</p> <p>21 server under the numbering system "BP" and then</p> <p>22 a number?</p> <p>23 A. No, they didn't exist under a "BP"</p> <p>24 number. They existed in the Pet Quarters files</p> <p>25 under probably various different subfolders</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 just don't know. I can't tell just by the name</p> <p>3 of the author.</p> <p>4 Q. Have you read any articles on the</p> <p>5 impact of various trading strategies on stock</p> <p>6 prices?</p> <p>7 A. I don't know exactly what you mean</p> <p>8 by that.</p> <p>9 Q. Well, I mean, when you -- when you</p> <p>10 prepared your report, you cite one article that</p> <p>11 you reviewed in your -- in Exhibit No. 2. I</p> <p>12 remember last night, as I was stumbling through</p> <p>13 the two-gigabyte file and I was not able to</p> <p>14 retract it, that I found another example --</p> <p>15 another sheet of material that you had</p> <p>16 considered, or somebody had purportedly</p> <p>17 considered, when they prepared the expert</p> <p>18 report. And it included a great number of</p> <p>19 other articles.</p> <p>20 Was there -- was there a lot of</p> <p>21 literature that you read to prepare your expert</p> <p>22 report that are not listed in what you</p> <p>23 considered there?</p> <p>24 MR. SOHN: In this case?</p> <p>25 MR. GUIDO: In this case.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 with different pieces of analysis in them.</p> <p>3 Q. Well, did the subfolders mention</p> <p>4 the subject matter of each of the files?</p> <p>5 A. I would have to go back and look</p> <p>6 at the folder to tell you that.</p> <p>7 Q. So you don't know. All right.</p> <p>8 A. I don't know sitting here.</p> <p>9 Q. The -- with regard to the issue of</p> <p>10 multiple statistical regressions, have you ever</p> <p>11 read any articles where he explains what was</p> <p>12 wrong with the Bonferroni adjustment?</p> <p>13 A. I've read articles that discuss</p> <p>14 the Bonferroni adjustment.</p> <p>15 Q. Have you ever read any article by</p> <p>16 Thomas Perneger, P-e-r-n-e-g-e-r?</p> <p>17 A. If you show me the article, I</p> <p>18 could look at it. I may have.</p> <p>19 Q. But you don't recall reading it?</p> <p>20 A. I don't recall that specific name,</p> <p>21 but I may well have read the article.</p> <p>22 Q. Have you ever -- are you aware of</p> <p>23 an article by Kenneth Rothman on no adjustments</p> <p>24 are needed for multiple comparisons?</p> <p>25 A. I may have read that article. I</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I can't recall seeing -- I can't</p> <p>3 recall creating an Exhibit 3, which would be</p> <p>4 the exhibit that details the documents</p> <p>5 reviewed, that lists a large number of</p> <p>6 articles. I just can't remember them being</p> <p>7 there.</p> <p>8 I do know that the Chaplinsky</p> <p>9 article was one I definitely reviewed in the</p> <p>10 context of performing this report.</p> <p>11 I am also just generally aware of</p> <p>12 other articles that I didn't refer to</p> <p>13 specifically for this report, but I -- that</p> <p>14 formed the background of my professional</p> <p>15 knowledge of FPS securities.</p> <p>16 Q. Well, let me ask you a question:</p> <p>17 Is there any literature or paper that you've</p> <p>18 read that supports the running of Regression</p> <p>19 Number 1 that you did in this case?</p> <p>20 A. A specific article or report?</p> <p>21 Q. Yeah.</p> <p>22 A. Not sitting here that I can think</p> <p>23 of one.</p> <p>24 Q. Is there any that supports the</p> <p>25 running of Regression Number 2?</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Let me look at what Regression</p> <p>3 Number 2 is.</p> <p>4 Well, generally there are articles</p> <p>5 that look at flags for whether someone is in</p> <p>6 the market or whether someone buys or sells.</p> <p>7 There are many articles that have flags for</p> <p>8 that, when looking at the impact of a trade.</p> <p>9 Q. Can you give us an example?</p> <p>10 A. Well, articles written by</p> <p>11 Professors Glosten and Jones have, in some of</p> <p>12 their regressions specifications, have flags</p> <p>13 for whether someone buys or whether someone</p> <p>14 sells -- or what they determine to be a</p> <p>15 seller-initiated trade or a buyer-initiated</p> <p>16 trade.</p> <p>17 And in much of the market</p> <p>18 microstructure literature, there are</p> <p>19 specifications that have flags or dummies for</p> <p>20 that type of -- for measuring that activity.</p> <p>21 Q. Well, in the literature that you</p> <p>22 saw simply flags for buys or sells, or buys</p> <p>23 that are identified as buys because they're at</p> <p>24 the offer and sells because they're at the bid?</p> <p>25 A. They're -- they're certainly --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 offer?</p> <p>3 A. I believe that's correct.</p> <p>4 Q. Okay. And -- but you didn't do</p> <p>5 that when you did your regression, did you?</p> <p>6 A. No. We -- we looked at Rhino's --</p> <p>7 whether Rhino just bought. We wanted to be as</p> <p>8 comprehensive as possible.</p> <p>9 Q. You didn't look to determine</p> <p>10 whether or not it was at the bid or the offer</p> <p>11 or where it was in that range?</p> <p>12 A. We did not do that.</p> <p>13 Q. Okay. Now, with regard to</p> <p>14 Regression Number 3, is there any literature</p> <p>15 that supports the running of Regression Number</p> <p>16 3?</p> <p>17 A. Well, all Regression 3 is, is --</p> <p>18 Regression 3 differs from Regression 2 by also</p> <p>19 looking at transfers in principal and direct</p> <p>20 purchases of stock. And there's certainly a</p> <p>21 lot of literature out there that tells you that</p> <p>22 when an entity issues stock, that is an</p> <p>23 important piece of information for the market.</p> <p>24 Q. Well, that's public issuances.</p> <p>25 Right? That literature --</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 they're certainly dummy variables. They don't</p> <p>3 have anything to do with volume. But, as I</p> <p>4 said in my last answer, based on a particular</p> <p>5 definition of what a buy is will determine</p> <p>6 whether that zero-one dummy is a buy or is a</p> <p>7 zero or a one.</p> <p>8 Now, there may be different</p> <p>9 definitions of how you define a buy that --</p> <p>10 that differ across the literature. I'm not</p> <p>11 certain whether there are or not.</p> <p>12 Q. Well, I mean in terms of the</p> <p>13 literature definitions of buy, do you know of</p> <p>14 any literature that uses your definition of</p> <p>15 buy? Just a simple buy as opposed to a</p> <p>16 transaction at the bid?</p> <p>17 A. There may be. I can't think of --</p> <p>18 Q. But you --</p> <p>19 A. I can't think of a piece of</p> <p>20 literature as I sit here.</p> <p>21 Q. But Mr. Glosten, Professor</p> <p>22 Glosten, has written papers on the use of</p> <p>23 analyzing trades by characterizing them as</p> <p>24 buys. And in those papers didn't he define</p> <p>25 buys as transactions at the bid -- at the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. It's public issuances of stock.</p> <p>3 But, again, if the market knows about it,</p> <p>4 because Rhino is a big player in this market,</p> <p>5 then that would, in turn, be an important piece</p> <p>6 of information for the market.</p> <p>7 Q. Okay. But you don't have any</p> <p>8 information that the Rhino or Amro purchases</p> <p>9 were -- was information that was available to</p> <p>10 the public?</p> <p>11 A. We did not do that determination,</p> <p>12 but that's -- that's part of the reason we're</p> <p>13 testing it, because we wanted to cover all our</p> <p>14 bases here.</p> <p>15 Q. Well, but if it turns -- one of</p> <p>16 the reasons that you could determine not to</p> <p>17 have a significance is that that information</p> <p>18 could have turned out not to have been</p> <p>19 available to the market. Isn't that true?</p> <p>20 A. Actually, that's wrong, because</p> <p>21 the more regressions you run, the in -- the</p> <p>22 more likely you are to get a spurious result.</p> <p>23 So you run an additional regression, the more</p> <p>24 likely you are to get a spurious result.</p> <p>25 Q. Well, is there an incentive to run</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 spurious regressions so that you could get a</p> <p>3 spurious result?</p> <p>4 A. A spurious result would be a</p> <p>5 result that has a "P" value of less than .05,</p> <p>6 which would, if interpreted incorrectly, would</p> <p>7 be viewed as price impact. And that is what</p> <p>8 we're trying to avoid here. We're trying to</p> <p>9 avoid data mining.</p> <p>10 Q. And one of the -- and one of the</p> <p>11 ways to do data mining is to run regressions</p> <p>12 that you know are going to result in no</p> <p>13 significant relationship, isn't it?</p> <p>14 A. No, I would say data mining is the</p> <p>15 opposite of that. I would say data mining is</p> <p>16 running regressions until you find a</p> <p>17 significant relationship and then that's</p> <p>18 your -- that's your model.</p> <p>19 Q. What was the first regression that</p> <p>20 was ever run of Sedona's stock price in</p> <p>21 relationship to Badian's activity?</p> <p>22 A. Well, I can't speak to that</p> <p>23 because if you're talking about -- well, are</p> <p>24 you talking about at FTI or are you talking</p> <p>25 about prior to FTI?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 report?</p> <p>3 A. I didn't search for any articles</p> <p>4 on the PIPEs market for this specific</p> <p>5 engagement. I was aware of, just based on my</p> <p>6 professional knowledge in the economics and</p> <p>7 finance literature, I've been aware of a number</p> <p>8 of articles out there that are -- that speak to</p> <p>9 future price securities. And I've talked about</p> <p>10 at least one of them earlier this morning.</p> <p>11 Q. I think one of them was an article</p> <p>12 by Hillion?</p> <p>13 A. Hillion and Vermaelen.</p> <p>14 MR. GUIDO: I'd like to have</p> <p>15 marked as the exhibit next number an article by</p> <p>16 Hillion and Vermaelen.</p> <p>17 (Whereupon, exhibit is received</p> <p>18 and marked BP-27 for identification.)</p> <p>19 BY MR. GUIDO:</p> <p>20 Q. Is this the article that you were</p> <p>21 referring to?</p> <p>22 A. Yes.</p> <p>23 Q. Does the paper exclude the</p> <p>24 possibility that someone would or could</p> <p>25 manipulate the stock price to take advantage of</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Ever.</p> <p>3 A. Well, I don't know.</p> <p>4 Q. You don't know.</p> <p>5 So Regression Number 5, the one</p> <p>6 that found the significant relationship, could</p> <p>7 have been the first regression that was run.</p> <p>8 Right?</p> <p>9 A. It certainly wasn't the first</p> <p>10 regression run. When we did our analysis at</p> <p>11 FTI, we ran all of the regressions.</p> <p>12 Q. Simultaneously or --</p> <p>13 A. We instructed for them all to be</p> <p>14 run.</p> <p>15 Q. Right. Okay. But that's after</p> <p>16 they had already been run once before.</p> <p>17 Right?</p> <p>18 A. That's -- that's after they had</p> <p>19 been run once before, but I'm not sure on the</p> <p>20 same time periods that we ran them on -- at</p> <p>21 FTI.</p> <p>22 Q. When -- did you search for any</p> <p>23 literature on the PIPEs market for financial</p> <p>24 future price securities other than the one</p> <p>25 article that you cite in your -- in your expert</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 a low conversion price?</p> <p>3 MR. SOHN: Does it say that that's</p> <p>4 not possible? Is that the question?</p> <p>5 MR. GUIDO: Yeah.</p> <p>6 A. Well, this is a 35-page article</p> <p>7 with -- and although I'm very aware of it, I</p> <p>8 don't know every single piece of analysis or</p> <p>9 conclusion they come to. So, I can't speak to</p> <p>10 that.</p> <p>11 I know, basically, the focus of</p> <p>12 the -- of the paper, the thrust of the paper,</p> <p>13 in my opinion, is to demonstrate the fact that</p> <p>14 floating price convertibles are issued by very</p> <p>15 risky firms and are, therefore, very risky for</p> <p>16 investors that hold them.</p> <p>17 Q. And isn't it -- does it also talk</p> <p>18 about the firm -- that they are firms that</p> <p>19 stock prices are very responsive to external</p> <p>20 events?</p> <p>21 A. It -- it may talk about that.</p> <p>22 You'd have to point me to exactly where that</p> <p>23 is. I can't recall that. But certainly the</p> <p>24 stock prices of these companies, just like</p> <p>25 Sedona's, are very volatile.</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Have you ever studied any</p> <p>3 literature on -- on the -- what's referred to</p> <p>4 as the scalping phenomenon in trading?</p> <p>5 A. The scalping phenomenon?</p> <p>6 Q. Uh-huh.</p> <p>7 A. I may have in the past. I can't</p> <p>8 remember sitting here.</p> <p>9 Q. Well, have you ever heard the term</p> <p>10 "pump and dump"?</p> <p>11 A. Yes.</p> <p>12 Q. In what context?</p> <p>13 A. In the context of the SEC bringing</p> <p>14 litigation against individuals for alleging</p> <p>15 pump-and-dump schemes.</p> <p>16 Q. Have you ever seen any statistical</p> <p>17 analyses or regression analyses of the impact</p> <p>18 of those pump-and-dump schemes?</p> <p>19 A. I haven't seen any statistical --</p> <p>20 do you mean statistical analyses on the</p> <p>21 frequency of them or -- the frequency of the</p> <p>22 suits or statistical analysis in a particular</p> <p>23 pump-and-dump --</p> <p>24 Q. Of the impact --</p> <p>25 A. -- scheme?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 financial innovations aimed at resolving</p> <p>3 asymmetrical information problems in small,</p> <p>4 risky firms. In theory, a floating price</p> <p>5 convertible is ideal for such firms. In</p> <p>6 practice, the stocks of such firms are illiquid</p> <p>7 and subject to manipulation by short sellers</p> <p>8 and hedge funds. The floating price</p> <p>9 convertible may, thus, produce a downwards</p> <p>10 spiral in the stock price."</p> <p>11 Do you see that?</p> <p>12 A. Yes.</p> <p>13 Q. Do you agree with it?</p> <p>14 A. Yeah, I think the stocks of such</p> <p>15 firms could be subject to manipulation. I</p> <p>16 don't rule that out.</p> <p>17 Q. Oh, okay. The -- on the</p> <p>18 Bonferroni adjustments, I'd like to hand you</p> <p>19 the Perneger article.</p> <p>20 MR. GUIDO: And may I have it</p> <p>21 marked as Exhibit No. 28?</p> <p>22 (Whereupon, exhibit is received</p> <p>23 and marked BP-28 for identification.)</p> <p>24 MR. SOHN: Do you have another</p> <p>25 copy?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Of the impact of them.</p> <p>3 A. I don't believe I have. I may</p> <p>4 have, but I can't remember.</p> <p>5 Q. Do you consider the production of</p> <p>6 this disk that I received at eight o'clock to</p> <p>7 be a timely disclosure under the court order in</p> <p>8 the subpoena issued against you in this case?</p> <p>9 MR. SOHN: Objection.</p> <p>10 A. I don't know what the time -- what</p> <p>11 would be considered a timely disclosure or not.</p> <p>12 It's a -- it's a disclosure. If there was a</p> <p>13 gap in what was produced before, I apologize.</p> <p>14 And we've produced to you a supplement. And,</p> <p>15 like I said, most, if not all, of what I</p> <p>16 produced to you I would consider to be not</p> <p>17 relevant to this case, but you're free to look</p> <p>18 at it.</p> <p>19 Q. Take a look at the Hillion</p> <p>20 article, which is Exhibit 27, at page 384. Do</p> <p>21 you see the paragraph that says, "This paper</p> <p>22 makes several contributions..."?</p> <p>23 A. Yes.</p> <p>24 Q. And the first one, it says, "It</p> <p>25 illustrates the difficulties of designing</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 MR. GUIDO: Oh, excuse me.</p> <p>3 MR. SOHN: Thank you.</p> <p>4 BY MR. GUIDO:</p> <p>5 Q. Have you ever read this Perneger</p> <p>6 article? Perneger.</p> <p>7 A. I may have. It looks somewhat</p> <p>8 familiar, but I can't say for certain.</p> <p>9 Q. Well, I think you testified</p> <p>10 earlier that one of the things that you did was</p> <p>11 apply the Bonferroni adjustment to determine</p> <p>12 that the Regression 5 was, I think, spurious, I</p> <p>13 think was your term?</p> <p>14 A. Spurious correlation.</p> <p>15 Q. Yeah.</p> <p>16 Can there be a spurious</p> <p>17 noncorrelation?</p> <p>18 A. Well, generally I think that's not</p> <p>19 the problem. I think the problem is spurious</p> <p>20 correlations.</p> <p>21 Q. I understand --</p> <p>22 A. So I'm not -- I'm not sure whether</p> <p>23 there could be or could not be in a</p> <p>24 hypothetical. But certainly there's not a</p> <p>25 spurious noncorrelation here since the vast</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 majority of all our results show no impact and</p> <p>3 the vast minority do. And, so, that would</p> <p>4 be -- that would be -- those would be the</p> <p>5 spurious correlations.</p> <p>6 Q. Well, is a -- is a spurious</p> <p>7 correlation one in which you have a variable</p> <p>8 that you don't know what -- whether it actually</p> <p>9 had an impact in the market, or could likely</p> <p>10 have an impact on the market?</p> <p>11 A. No, that's not a spurious</p> <p>12 correlation. Not the way you asked that</p> <p>13 question.</p> <p>14 Q. What if Andreas Badian had -- had</p> <p>15 lent Sedona \$35 million in cash and it wasn't</p> <p>16 public? And you included that in your</p> <p>17 regression analysis on the stock price of</p> <p>18 Sedona. Would that be a spurious</p> <p>19 regression?</p> <p>20 MR. SOHN: Objection. The</p> <p>21 question is whether he lent a public company</p> <p>22 money and it wasn't publicly known that he lent</p> <p>23 the public company money?</p> <p>24 MR. GUIDO: That's correct.</p> <p>25 A. I can't answer the question the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 legitimate.</p> <p>3 Q. So, you're saying the Bonferroni</p> <p>4 method is less legitimate when there are large</p> <p>5 number of tests that are being looked at?</p> <p>6 A. May be more problematic when you</p> <p>7 have thousands of tests or large numbers of</p> <p>8 tests.</p> <p>9 Q. And not when you have a smaller</p> <p>10 number of tests?</p> <p>11 A. Right. That's just the way the --</p> <p>12 the statistics work. And that's -- that's</p> <p>13 verified in the literature. I mean, that's</p> <p>14 talked about in the literature, Bonferroni.</p> <p>15 Q. Really? What literature?</p> <p>16 A. I can't cite an article right off</p> <p>17 the top of my head, but I do understand that's</p> <p>18 part of the issue, or that's part of the</p> <p>19 literature.</p> <p>20 Q. Well, I mean, this article,</p> <p>21 okay -- take a look at the paragraph that says</p> <p>22 "Adjustment for multiple tests."</p> <p>23 How many tests are being addressed</p> <p>24 there?</p> <p>25 A. In this example, it's 20.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 way you've asked it. It just doesn't make any</p> <p>3 sense.</p> <p>4 Q. Okay. Now, let's go -- let's take</p> <p>5 a look at the Perneger article. It says -- and</p> <p>6 there's a number of points. See the blue?</p> <p>7 A. Yes.</p> <p>8 Q. That says "Adjusting Statistical</p> <p>9 Significance for the number of tests that have</p> <p>10 been performed on study data -- the Bonferroni</p> <p>11 method -- creates more problems than it</p> <p>12 solves."</p> <p>13 Do you agree or disagree with</p> <p>14 that?</p> <p>15 A. I disagree with that in the sense</p> <p>16 that this is an article designed pri -- it</p> <p>17 looks solely for biomedical research, where</p> <p>18 typically you have very, very large numbers of</p> <p>19 tests performed. And, therefore, the</p> <p>20 Bonferroni method may be more problematic</p> <p>21 there.</p> <p>22 But for the types of cases that I'm</p> <p>23 involved in or that don't involve those types</p> <p>24 of -- those numbers of tests. And, therefore,</p> <p>25 I think the Bonferroni method is perfectly</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. How many were you talking about?</p> <p>3 A. I'm talking about nine or 18</p> <p>4 regressions.</p> <p>5 Q. Okay. Well, this article is</p> <p>6 addressing nine -- I mean 20 trials.</p> <p>7 Is that a significantly larger</p> <p>8 number than the 18 or 19 that you conducted?</p> <p>9 A. This example isn't, but my</p> <p>10 understanding is that the literature talks</p> <p>11 about the Bonferroni adjust -- or correction</p> <p>12 being problematic when you have very large</p> <p>13 numbers of tests.</p> <p>14 Q. Well, doesn't this article talk</p> <p>15 about Bonferroni adjustments being problematic</p> <p>16 when there are 20 independent tests that are</p> <p>17 being performed?</p> <p>18 A. Well, I would have to read the</p> <p>19 whole article to understand it, but my</p> <p>20 understanding is that this is an article that's</p> <p>21 focused on biomedical research or epit --</p> <p>22 epitomology, not the types of issues that we're</p> <p>23 dealing with here.</p> <p>24 Q. What difference does it make if</p> <p>25 you're just talking about application of</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 mathematical statistical analyses what -- what</p> <p>3 you're looking at?</p> <p>4 A. Well, one difference is that we're</p> <p>5 looking at a universal null here. We're</p> <p>6 looking at is there a pricing impact or not,</p> <p>7 regardless of the channel? And this article</p> <p>8 itself says that a Bonferroni adjustment may be</p> <p>9 appropriate in those cases.</p> <p>10 Q. Wait a minute. You're saying that</p> <p>11 you're looking at is there a price impact or</p> <p>12 not?</p> <p>13 A. Yes.</p> <p>14 Q. I thought what we were looking at</p> <p>15 is could you reject the null hypothesis that</p> <p>16 there was a price impact?</p> <p>17 A. Fine. If you want to put it that</p> <p>18 way, we're looking at a null hypothesis,</p> <p>19 universal null, which is, is there a price</p> <p>20 impact or not? Or is there a price -- the null</p> <p>21 hypothesis being no impact. That's the</p> <p>22 universal null that we're looking at.</p> <p>23 We can test that in a number of</p> <p>24 different ways. And that's -- that's what</p> <p>25 we're doing here. There's no pre-established,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 these --</p> <p>3 Q. Failing to reject the null when it</p> <p>4 is false.</p> <p>5 A. Yes, that's right. Yeah. Now</p> <p>6 you've said it and I agree. It's very late.</p> <p>7 Q. So, failing to reject the null.</p> <p>8 Isn't that what the 15 regressions did in your</p> <p>9 analyses here?</p> <p>10 A. That's what all of the regressions</p> <p>11 did.</p> <p>12 Q. Well, 15 of the 18. Three of them</p> <p>13 showed that there was a significant</p> <p>14 correlation, which you indicated you think are</p> <p>15 spurious. But 15 of them failed to reject the</p> <p>16 null. Right?</p> <p>17 A. I would disagree with that. I</p> <p>18 would say all of them failed to reject the null</p> <p>19 when you properly adjust for the spurious</p> <p>20 correlation property.</p> <p>21 Q. Okay. But if you do the</p> <p>22 adjustment, okay, doesn't it increase the</p> <p>23 likelihood of the results that the null</p> <p>24 hypothesis has not been rejected? Does it</p> <p>25 increase the error?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 specific hypothesis about exactly how the</p> <p>3 transmission mechanism would go from a Badian</p> <p>4 or a Rhino trade to the Sedona stock price.</p> <p>5 Q. What's the --</p> <p>6 A. And, therefore, so there's no</p> <p>7 specific transmission mechanism. There's lot</p> <p>8 of potentially different ones.</p> <p>9 Q. Okay. What's a Type II error?</p> <p>10 A. A Type II error is the opposite of</p> <p>11 a Type I error. Type I error is rejecting the</p> <p>12 null when it's true, and a Type II error is</p> <p>13 failing to reject the null when it's false.</p> <p>14 Q. Okay. And does the application of</p> <p>15 the Bonferroni method increase the likelihood</p> <p>16 of a Type II error?</p> <p>17 A. It generally increases the</p> <p>18 likelihood of a Type II error and decreases the</p> <p>19 likelihood of a Type I error.</p> <p>20 Q. And the Type II error being a</p> <p>21 finding of no significance?</p> <p>22 A. A Type II error is failing to</p> <p>23 reject the null when it is -- I'm sorry. It's</p> <p>24 very late. Failing to reject the null when it</p> <p>25 is false. Yes. I got that right. There's all</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. No, what it does is it restores</p> <p>3 the Type I error to the original Type I error</p> <p>4 rate that you would expect from just running</p> <p>5 one regression. You want to restore the Type I</p> <p>6 error rate to 5 percent, and that's what the</p> <p>7 Bonferroni correction does.</p> <p>8 Q. Based on the use of regression</p> <p>9 analyses that may generate a false result</p> <p>10 themselves.</p> <p>11 A. I don't know what you're talking</p> <p>12 about.</p> <p>13 Q. Well, isn't it true -- isn't it</p> <p>14 true that any one of these regression analyses</p> <p>15 could have resulted in a false result?</p> <p>16 MR. SOHN: Objection to the</p> <p>17 form.</p> <p>18 A. I don't know what you mean by a</p> <p>19 "false result."</p> <p>20 Q. A false positive significance, a</p> <p>21 false negative significance.</p> <p>22 A. There's always an error of -- in</p> <p>23 all statistics, there's always an error of a</p> <p>24 false positive or a false negative. The</p> <p>25 generally accepted way of going about any kind</p>

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<p>1 - STEPHEN D. PROWSE - 2 of statistical analysis is to set the Type I 3 error at 5 percent, and that's what the 4 Bonferroni correction does when you're doing 5 multiple comparisons. 6 Q. The -- remember I asked you a 7 question about the powers of tests? 8 A. I believe so. 9 Q. Now, isn't it true that if you do 10 a regression and you find the results are not 11 significant and the null hypothesis is not 12 rejected, one of the reasons that this can 13 happen is because the null hypothesis is false, 14 but by chance the data happened to be of the 15 kind expected under the null hypothesis? 16 A. That is certainly a possibility. 17 Q. If the power of the test is low, 18 is this more likely to be possible? 19 A. If the power of the test is low, 20 then the chances of a Type II error are higher, 21 yes, I believe. 22 Q. Okay. And if the study that has 23 low power fails to show a significant effect, 24 are the results more fairly described as 25 inconclusive than as negative?</p>	<p>1 - STEPHEN D. PROWSE - 2 analysis? 3 Q. Yeah, with regard to any 4 particular regression. What does low power 5 mean? 6 A. Low power means a higher level of 7 Type II error. 8 Q. And the Type II error being that 9 you find that you can't reject the null 10 hypothesis when the null hypothesis should be 11 rejected? 12 A. Failure to reject the null when 13 the null is false, right. 14 Q. Okay. 15 MR. SOHN: Mr. Guido, I think 16 we've hit seven. 17 MR. GUIDO: One more question. 18 BY MR. GUIDO: 19 Q. Did you attempt to determine what 20 the probability of accepting the false on a 21 null hypothesis was in any of your regressions? 22 A. Did I attempt to -- no. I mean, I 23 attempted to fix the probability of a Type II 24 error at the generally accepted level. 25 MR. GUIDO: Okay. No further</p>
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<p>1 - STEPHEN D. PROWSE - 2 A. I'm sorry, I missed that. 3 Q. When a study with low power fails 4 to show a significant effect, are the results 5 more fairly described as inconclusive than 6 negative? 7 MR. SOHN: Objection to the form. 8 A. I'd have to think about that. 9 Q. Have you ever thought about it 10 before? 11 A. Not exactly in those words, but -- 12 so I'd have to think about it. 13 Q. Well, when was the last time you 14 read the Kaye-Freedman piece? 15 A. What piece are you talking about? 16 Q. The piece that you cited from 17 the -- what is it? The section on statistics 18 from the -- from the judiciary. 19 A. Not -- certainly not within the 20 last few weeks or months. 21 Q. Well, did you read it when you 22 were preparing your report? 23 A. No. I was aware of it. 24 Q. What is a low power? 25 A. With regards to a statistical</p>	<p>1 - STEPHEN D. PROWSE - 2 questions. 3 MR. SOHN: Mr. Guido, I just, you 4 know, expected that you will instruct your 5 colleagues who are here today to maintain their 6 notes, whatever they've been writing. 7 MR. DUNBAR: Could we go off the 8 record? Is that really what you meant to say? 9 MR. GUIDO: About the -- I'm 10 sorry, Fred. You're not asking the questions. 11 THE VIDEOGRAPHER: This concludes 12 the videotaped deposition of Dr. Stephen Prowse 13 consisting of five videotapes. Going off the 14 record at 6:56 p.m. 15 (Whereupon, the deposition 16 concluded at 6:56 p.m.) 17 18 19 20 21 22 23 24 25</p>

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<p style="text-align: right;">Page 338</p> <p>1 CERTIFICATE OF DEPONENT</p> <p>2 I hereby certify that I have read and examined the</p> <p>3 foregoing transcript, and the same is a true and</p> <p>4 accurate record of the testimony given by me.</p> <p>5 Any additions or corrections that I feel are</p> <p>6 necessary, I will attach on a separate sheet of</p> <p>7 paper to the original transcript.</p> <p>8</p> <p>9</p> <p>10</p> <p>11 _____</p> <p>12 Signature of Deponent</p> <p>13</p> <p>14 I hereby certify that the individual representing</p> <p>15 himself/herself to be the above-named individual,</p> <p>16 appeared before me this _____ day of _____,</p> <p>17 2010, and executed the above certificate in my</p> <p>18 presence.</p> <p>19</p> <p>20</p> <p>21 _____</p> <p>22 NOTARY PUBLIC IN AND FOR</p> <p>23</p> <p>24 _____</p> <p>25 County Name</p> <p>MY COMMISSION EXPIRES:</p>	
<p style="text-align: right;">Page 339</p> <p>1 CERTIFICATE</p> <p>2</p> <p>3 I, Bridget Lombardozi, Certified</p> <p>4 Shorthand Reporter and Notary Public, hereby</p> <p>5 certify that the foregoing is a true and</p> <p>6 accurate transcript of the deposition of said</p> <p>7 witness who was first duly sworn by me on the</p> <p>8 date and place hereinbefore set forth.</p> <p>9</p> <p>10 I FURTHER CERTIFY that I am neither</p> <p>11 attorney nor counsel for, nor related to or</p> <p>12 employed by, any of the parties to the action</p> <p>13 in which this deposition was taken and further</p> <p>14 that I am not a relative or employee of any</p> <p>15 attorney or counsel employed in this action,</p> <p>16 nor am I financially interested in this case.</p> <p>17</p> <p>18 Dated this 7th day of March, 2010.</p> <p>19</p> <p>20</p> <p>21 _____</p> <p>22 Bridget Lombardozi</p> <p>23 Certified Realtime Reporter - NCRA</p> <p>24 Certified Shorthand Reporter</p> <p>25 New York Notary Public</p>	